93-84

No. ——

Supreme Court, U.S.
FILED
JUL 15 1993
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

SHELL OIL COMPANY,
Petitioner,

v.

EDWARD L. NELSON, *et al.*,
Respondents.

Petition for a Writ of Certiorari to the Court of Appeal for the State of California, Second Appellate District, Division One

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PETITION FOR A WRIT OF CERTIORARI

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July 15, 1993

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTIONS PRESENTED

1. Whether the California punitive damages system denied Shell Oil Company ("Shell") its right to procedural due process under the Due Process Clause of the Fourteenth Amendment to the United States Constitution ("Due Process Clause") by granting excessive discretion to the fact finder through subjective and ill-defined criteria for awarding punitive damages and by its extremely deferential "passion or prejudice" standard of appellate review of punitive damages awards.

2. Whether the California courts have denied Shell its right to substantive due process under the Due Process Clause by imposing a fundamentally unfair punitive damages award against Shell and by more than doubling the award (after successful appeals by Shell) based on essentially the same factual record.

3. Whether the punitive damages award in this case violates Shell's right to due process because the geometric increase in punitive damages based on the plaintiffs' attorney's fees was unreasonable and irrational in light of the purposes of punitive damages in California.

PARTIES TO THE PROCEEDING

The Petitioner, Shell Oil Company, is a Delaware corporation with its principal place of business in Houston, Texas. A listing of parent corporations and non-wholly owned subsidiaries of Shell Oil Company is included in the Appendix to this Petition at p. 63a.

The Respondents are Edward L. Nelson; Charlotte Louise Nelson; Edward L. Nelson and Charlotte Louise Nelson as trustees of the Nelson Trust.

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PETITION FOR A WRIT OF CERTIORARI

Shell Oil Company petitions for a Writ of Certiorari to review the judgment of the Court of Appeal for the State of California, Second Appellate District, Division One.

OPINIONS BELOW

The decision of the Court of Appeal for the State of California, Second Appellate District, Division One is unreported. Pet. App. 2a-24a.[1] That opinion affirmed the decision of the trial court to award against Shell $4.6 million in punitive damages and $268,891 in "actual" damages, which consisted almost entirely of attor-

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[1] Citations to the Appendix to the Petition for Certiorari will be styled "Pet. App. —a."

ney's fees. The statement of decision of the trial court is unreported. Pet. App. 25a-33a. The trial court's statement of decision was entered after the Court of Appeal, on a prior appeal by Shell, vacated and remanded an earlier punitive damages award. Pet. App. 9a-10a.

JURISDICTION

The judgment of the trial court was rendered March 31, 1992. Pet. App. 25a-27a. The trial court denied Shell's motion to vacate on May 4, 1992. Pet. App. 35a. The decision of the California Court of Appeal was rendered February 26, 1993. Pet. App. 2a. The Court of Appeal denied Shell's petition for rehearing on March 22, 1993. Pet. App. 34a. Shell timely petitioned the Supreme Court of California to review the decision of the Court of Appeal, and that Court denied review on May 26, 1993. Pet. App. 1a. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISION INVOLVED

The Fourteenth Amendment to the Constitution of the United States provides in part: "No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any state deprive any person of life, liberty, or property, without due process of law . . . ."

STATEMENT

The convoluted, conflicting history of the treatment of this case by the California courts goes far toward showing that Shell's right to due process has been violated. This case has seen decisions by three different panels of the California Court of Appeal (the intermediate appellate court in California). Pet. App. 2a, 9a-10a. Four different awards of punitive damages have been ordered. These awards have ranged in amount from the jury's original award of $235,600 to a high of $6.295 million.

Pet. App. 8a-10a. The current punitive award, determined by the trial court, stands at $4.6 million, which bears a relationship of 750-to-1 to the compensatory damage award of only $6,133. Pet. App. 10a, 56a.

On June 18, 1985, the State of California filed a Complaint in Eminent Domain on a Los Angeles property located in the path of the well-publicized Century Freeway Project. Pet. App. 8a. The complaint in Eminent Domain named the following defendants: Edward L. Nelson, Charlotte Louise Nelson; Edward L. Nelson and Charlotte Louise Nelson as trustees of the Nelson Trust (collectively "Nelson Trust"); and Shell Oil Company ("Shell"). Pet. App. 8a. Nelson Trust owned the fee interest in the property, while Shell owned a leasehold interest under a fixed-term lease. Pet. App. 5a. Shell valued its leasehold interest at $620,000. Pet. App. 7a.

On September 4, 1985, Nelson Trust answered the State's Complaint in Eminent Domain and filed a cross-complaint against Shell. Nelson Trust's primary allegation against Shell was that in negotiating several option agreements to extend the lease, Shell had not advised Nelson Trust of the planned construction of the Century Freeway and the resulting possibility that Nelson Trust's property would be condemned. Pet. App. 5a-7a. Shell, however, contended that the Freeway project had long been "public knowledge" and the trial court so found. Pet. App. 39a. Another of Nelson Trust's contentions was that Shell's base lease manual prescribed fraudulent and manipulative procedures to be used in negotiating commercial leases. Pet. App. 6a.

At the time of the taking of Nelson Trust's property by the State, Shell had not yet exercised the lease extension options. Pet. App. 4a, 7a. At that time, Shell still possessed the property under its original lease, the validity of which was not in issue. Pet. App. 4a, 7a.

On July 27, 1987, the jury returned its verdict in favor of Shell on Nelson Trust's claims for infliction of emotional distress and concealment of material facts with intent to defraud, but found Shell liable on Nelson Trust's claim for intentional misrepresentation. Pet. App. 8a, 39a. The jury awarded Nelson Trust $154,150 in actual damages, and $235,600 in punitive damages. Pet. App. 8a, 39a.

In addition to the causes of action heard by the jury, the trial court simultaneously heard Nelson Trust's equitable claim for rescission of the lease extension options. The trial court rescinded the options. Pet. App. 8a, 39a-40a.

The trial court went on to award punitive damages against Shell on Nelson Trust's recission cause of action in the amount of $1,887,375 (calculated on the basis of $1.9 million, less $5,625 in rental overpayments made by Shell to Nelson Trust, and less $7,000 for the value of Shell's remaining leasehold which was taken by the State in the condemnation proceedings). Pet. App. 8a, 40a. Shell appealed from both the jury verdict and the trial court's judgment of rescission. Pet. App. 9a, 40a.

During the course of the appeal, Nelson Trust elected the remedy of rescission. Pet. App. 9a, 40a. The Court of Appeal affirmed the judgment of rescission but vacated the award of punitive damages on the ground that under California law punitive damages cannot be awarded in the absence of actual damages, and no actual damages had been proved or awarded on the rescission count. Pet. App. 9a, 40a.

On remand, the trial court allowed Nelson Trust to offer evidence both of actual damages and of whether Shell had engaged in continuing wrongful conduct. Pet. App. 9a, 40a. The trial court then awarded $352,242 in general damages, the majority of which ($275,208) consisted of attorney's fees. Pet. App. 9a, 40a. The trial court also increased its original $1,887,375 punitive damages

award over three-fold to $6.295 million. Pet. App. 9a. In addition to relying on evidence introduced at the first trial, the trial court based its second punitive award on its conclusion that Shell had not withdrawn the base lease manual following the first award of punitive damages. Pet. App. 11a-12a. Shell appealed from the trial court's judgment. Pet. App. 9a.

On Shell's second appeal, a different panel of the Court of Appeal reduced the general damages award to $6,133 in lost interest income and $275,208 in attorney's fees. Pet. App. 9a, 40a-41a. The Court of Appeal also vacated the trial court's $6.295 million punitive damages award, holding that there was no evidence from which to conclude that Shell continued to use the base lease manual or the procedures in it after the first award of punitive damages Pet. App. 11a-12a.

The Court of Appeal remanded for the trial court's consideration of punitive damages "consistent with the views expressed in this opinion." Pet. App. 9a. The trial court was instructed not to hold yet another trial. Pet. App. 9a.

In its latest ruling, the trial court ordered that Shell pay $4.6 million in punitive damages to Nelson Trust. Pet. App. 10a, 27a. In making this final judgment, the trial court relied on the same factual conclusions that the Court of Appeal previously overturned as unsupported by the evidence. The trial court insisted that "in the absence of any written directives Shell undertook no meaningful or effective efforts to communicate any rescission of its prior policy as set forth in the manual," and speculated that "persons in the field" could still use the manual. Pet. App. 13a-14a.

Despite the internal inconsistency of the trial court's reasoning and its conflict with the Court of Appeal's October 1991 ruling, still a different panel of the Court of Appeal on February 26, 1993 applied California's virtually standardless, highly deferential "passion or preju-

dice" review and affirmed the trial court's $4.6 million punitive damages award. Pet. App. 17a, 24a. In so ruling, the Court of Appeal adopted the trial court's internally inconsistent reasoning as its own. Forced to concede in light of the ruling of the prior panel of the Court of Appeal in October of 1991 that there was no evidence that Shell continued to use the base lease manual, the Court of Appeal nevertheless ruled that an award of $2.7 million higher than the trial court's original $1.9 million award was supported because there was no evidence in the record that Shell had rescinded the manual in writing. Pet. App. 14a-15a, 18a-19a. In addition, the Court of Appeal rejected Shell's constitutional challenges to the punitive damages award and to California's deferential standard for appellate review of the award. Pet. App. 21a-24a.

On March 15, 1993, Shell filed a Petition for Rehearing, taking issue with the Court of Appeal's consideration of attorney's fees as part of compensatory damages for purposes of determining whether the ratio of punitive to compensatory damages was excessive. Pet. App. 42a. Shell pointed out that this excessiveness calculus was contrary to the purposes served by punitive damages awards under California law and violated due process. Pet. App. 42a, 56a-61a. The Court of Appeal denied the Petition for Rehearing on March 22, 1993. Pet. App. 34a.

Shell filed a timely Petition for Review with the California Supreme Court on April 7, 1993. Pet. App. 37a-62a. In this Petition Shell raised the same issues as are raised here. Pet. App. 38a. The California Supreme Court rejected Shell's Petition for Review on May 26, 1993. Pet. App. 1a.

REASONS FOR GRANTING THE PETITION

This case illustrates the failure of California's punitive damages system to comply with the dictates of due process and meaningfully constrain the arbitrary discretion of fact finders. California's inadequate procedures have al-

lowed punitive damages to "run wild." *Pacific Mutual Life Insurance Co. v. Haslip,* 499 U.S. 1, 111 S.Ct. 1032, 1043, 113 L.Ed2d 1, 20 (1991). There have been four different awards of punitive damages in this case based on essentially the same evidence A jury originally heard Nelson Trust's evidence of the alleged fraud by Shell in the negotiation of a commercial lease that underlies this case; that jury awarded Nelson Trust $235,600 in punitive damages. Yet Shell now comes before this Court with a $4.6 million punitive award having been ordered by the trial court, affirmed by the Court of Appeal and approved *sub silentio* by the California Supreme Court.

California applies a "passion or prejudice" review of punitive damages awards that is even less rigorous than the Kentucky standard of review, which this Court recently ordered the Kentucky Supreme Court to reconsider in light of *TXO Production Corp. v. Alliance Resources,* 61 U.S.L.W. 4766 (U.S. June 22, 1993). *H.C. Hanson v. American National Bank & Trust Co.,* 844 S.W.2d 408 (Ky. 1992), vacated 61 U.S.L.W. 3669 (U.S. June 28, 1993). The standard of review that was announced and applied by the Kentucky court in *American National Bank,* like the review applied by the California Court of Appeal in this case, focused only on whether the jury's decision was "free of passion or prejudice." 844 S.W.2d at 416.

As in Kentucky, California appellate review is extremely cursory because on appeal "[a]ll presumptions favor the correctness of the verdict and judgment," and the trial court's determination that a punitive damages award is not excessive is "accorded great weight." *Devlin v. Kearny Mesa AMC/Jeep/Renault, Inc.,* 155 Cal.App. 3d 381, 388, 202 Cal.Rptr. 204 (1984). Moreover, the factors considered by California courts in making and reviewing punitive damages awards are vague and considerably less specific than the factors considered in Kentucky. *See* p. 15, *infra.* This Court should grant certiorari, vacate the judgment, and remand here for all the

reasons this Court issued those orders in *American National Bank*.

This case also presents a compelling example of a grossly excessive punitive award that violates the substantive component of due process—the Constitution's guarantee of fundamental fairness. The trial court's $4.6 million punitive award against Shell in general, and the $2.7 million post-appeal increase in the punitive award in particular, bear no understandable relationship to the award by the jury, an independent fact finder in this same case, or to actual damages. The ratio of punitive damages to actual damages is more than 750-to-1, and the ratio of the $2.7 million post-appeal increase on the punitive award alone to actual damages is more than 440-to-1. This $2.7 million increase is not supported by any rationale that would satisfy the " 'general concern of reasonableness.' " *TXO*, 61 U.S.L.W. at 4770 (quoting *Haslip*, 499 U.S. at 18), required by due process. At a minimum the post-appeal $2.7 million increase in the punitive award against Shell is unsupportable, and this Court should vacate the judgment below and remand for reconsideration in light of *TXO*.

Finally, the punitive damages award in this case violates the Due Process Clause because the Court of Appeal improperly included Nelson Trust's attorney's fees within "actual" damages when calculating the ratio of punitive to actual damages. As a result of this erroneous procedure, punitive damages against Shell have been inflated many-fold without reference to, and in utter disregard of, the purposes for award of punitive damages in California. This Court should grant certiorari to consider the constitutional propriety of increasing punitive damages geometrically by means of an "excessiveness" calculus that does not ensure adherence to the state's criteria for award of punitive damages.

I. CALIFORNIA'S SYSTEM FOR ASSESSING PUNITIVE DAMAGES, ON ITS FACE AND AS APPLIED IN THIS CASE, HAS VIOLATED SHELL'S RIGHT TO PROCEDURAL DUE PROCESS BY VIRTUE OF ITS SUBJECTIVE, VAGUE CRITERIA FOR ASSESSING PUNITIVE DAMAGES AND DEFERENTIAL "PASSION OR PREJUDICE" STANDARD OF REVIEW

In *Haslip* this Court held that while punitive damages are not *"per se"* unconstitutional, "unlimited jury discretion—or unlimited judicial discretion for that matter—in the fixing of punitive damages may invite extreme results that jar one's constitutional sensibilities." *Haslip*, 111 S.Ct. at 1043. Only if "the discretion is exercised within reasonable constraints . . . [is] due process . . . satisfied." *Id.* at 1044. In *TXO*, a majority of this Court re-emphasized that to be supportable punitive damages awards must be the product of fair and reasonable procedures. *TXO*, 61 U.S.L.W. at 4769 (plurality opinion); *id.* at 4780 (O'Connor, J., dissenting) (rejecting the West Virginia Supreme Court of Appeal's "cavalier standards" and failure to apply "searching review"). In the instant case California's vague and "cavalier" standards for imposing punitive damages have joined with its cursory appellate review of such awards to deprive Shell of its right to procedural due process.

Under California law fact finders are entrusted with extremely broad discretion to inflict punitive damages. "The channeling of just the correct quantum of bile to reach the correct level of punitive damages is, to put it mildly, an unscientific process complicated . . . by the lack of objective criteria from either the Legislature or the courts as to 'how much' is necessary to punish and deter." *Devlin v. Kearny Mesa AMC/Jeep/Renault, Inc.*, 155 Cal.App.3d 381, 388, 202 Cal.Rptr. 204 (1984).

Although fifteen years ago the California Supreme Court pronounced three broad areas of inquiry as relevant

to the assessment of punitive damages, *Neal v. Farmers Insurance Exchange,* 21 Cal.3d 910, 928, 148 Cal.Rptr. 389, 582 P.2d 980 (1978), these considerations provide no meaningful limitation on a fact finder's discretion. Pursuant to *Neal,* fact finders are to assess punitive damages by reference to: (1) the nature of the defendants' conduct; (2) the relationship of punitive damages to actual damages; and (3) the defendant's financial condition. *Id.*; *see also Adams v. Murakami,* 54 Cal.3d 105, 110, 284 Cal. Rptr. 318, 813 P.2d 1348 (1991). As these areas of inquiry have developed under California law, they are either vague and highly subjective, or constitutionally unacceptable.

First, California's consideration of the nature of a defendant's conduct has not evolved to become a basis for consistency or predictability. In California, one fact finder may perceive a set of facts as an arms-length commercial transaction between two relatively sophisticated parties, albeit one in which some overreaching may have occurred. Since such overreaching was purely limited to financial dealings and did not imperil life or limb, such a fact finder may conclude that a relatively modest punitive award is justified. Another fact finder, *based on precisely the same set of facts,* may react viscerally to a large corporation's commercial dealings with an individual and impose punitive damages in the millions.

This scenario is precisely what occurred in this case. The jury in this case awarded a sum of only $235,600 in punitive damages. At trial the judge observed precisely the same evidence as the jury, but apparently perceived a far more grievous wrong and awarded $1.9 million in punitive damages. After that $1.9 million award was overturned, the trial court attempted unsuccessfully to triple the $1.9 million award and now successfully has more than doubled it. In California consideration of the nature of a defendant's conduct provides no constraint on entirely inconsistent punitive awards even within the same case.

The ratio of punitive damages to actual damages also might have evolved as a significant constraint on the arbitrary nature of California's punitive damages system, but it has not so evolved. For example, in *Gagnon v. Continental Casualty Co.*, 211 Cal.App.3d 1598, 260 Cal.Rptr. 305 (1989), the California appellate court held that the relationship between compensatory and punitive damages had little meaning and that a ratio of punitive to actual damages of "2,000 to 1 [has] been found reasonable." *Id.* at 1604. In this very case the ratio of punitive damages to actual damages is 750 to 1. Indeed, the ratio of just the *post-appeal increase* in punitive damages to actual damages is *440-to-1*, though this post-appeal increase itself is not justifiable. The evolution of this case makes clear that under California law consideration of the ratio of punitive damages to actual damages imposes little restraint on a fact finder's discretion.

With respect to California's third factor—the requirement that evidence of financial condition be introduced—this Court has recognized that use of a defendant's wealth to justify inflated punitive awards may violate the defendant's due process rights. In *TXO* this Court stated: "We agree with [defendant] that the emphasis on the wealth of the wrongdoer increased the risk that the award may have been influenced by prejudice against large corporations, a risk that is of special concern when the defendant is a nonresident." 61 U.S.L.W. at 4771; *id.* at 4779 (O'Connor, J., dissenting); *Haslip*, 111 S.Ct. at 1045 (plaintiffs must not be allowed to "enjoy a windfall because they have the good fortune to have a defendant with a deep pocket.").[2] In short, the *Neal* considera-

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[2] Unlike the Alabama scheme at issue in *Haslip*, which precludes the fact finder from considering the defendant's wealth when calculating punitive damages, *Haslip*, 111 S.Ct. at 1045 (in Alabama, evidence of the defendant's financial condition is only admitted during the post-verdict hearing conducted by the trial judge to determine whether the award is excessive), the California system not only encourages but requires the fact finder to do so.

tions are no more than "vague and amorphous guidance." *TXO*, 61 U.S.L.W. at 4774 (O'Connor, J., dissenting).

This case plainly demonstrates the failure of California law to constrain fact finder discretion in assessing punitive damages. Even though the same facts have predominated throughout the history of this case, and the same trial judge has presided throughout, this case has seen four awards of punitive damages which have differed from each other by as much as twenty-seven fold.

Indeed, the current punitive award is almost twenty times the jury's original punitive award in this same case, and is more than double the amount of even the trial court's initial punitive award. Yet the jury's award was based on essentially identical facts. The only new evidence since the jury's original award of $235,600 was evidence offered by Nelson Trust as to the possible continued use by Shell of its base lease manual after the first award of punitive damages. This evidence was so inconclusive that the Court of Appeal held in its October, 1991 opinion (reversing the trial court's award of $6.295 million in punitive damages), "[i]t is equally reasonable to conclude on the basis of what was testified to that Shell no longer uses the manual or the procedures it espouses." Pet. App. 12a.

The extraordinarily broad discretion of California fact finders is not counter-balanced by meaningful appellate review of punitive awards; California's standard of review cannot pass muster under the prior decisions of this Court. This Court expressly has warned that the sufficiency of punitive damages systems in several states is suspect, singling out Vermont and Mississippi, due to their inadequate standards for appellate review. *Haslip*, 111 S.Ct. at 1045 n.10 (questioning systems of review in which an award only "would be considered excessive when 'it evinces passion, bias and prejudice on the part of the jury so as to shock the conscience.' ") (citations omitted).

In *Adams v. Murakami*, the California Supreme Court itself expressed concern that California's highly differential appellate review cannot pass constitutional muster: "Although the high court upheld Alabama's punitive damages system . . ., the [*Haslip*] court expressed concern with less detailed state standards. . . . The California standard of review appears to be similar to those as to which the high court noted its concern." *Adams*, 54 Cal. 3d at 118, n.9.[3]

Thus, even the California Supreme Court has suggested that California's standard for appellate review of punitive damages awards does not meet the requirements of due process, because of the extraordinarily high standard that must be met before a punitive damages award will be disturbed on appeal. On appeal, "[a]ll presumptions favor the correctness of the verdict and judgment," *Devlin*, 155 Cal.App.3d at 388, and the trial court's determination that a punitive damages award is not excessive is "accorded great weight." *Id.* A "punitive damages award will be set aside only when it 'is so grossly

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[3] Several post-*Haslip* decisions from outside of California have concluded that pre-*Haslip* regimes for awarding punitive damages are inadequate to satisfy due process. (See *Johnson v. Hugo's Skateway*, 949 F.2d 1338, 1350-1351 (4th Cir. 1991); *Garnes v. Flemming Landfill, Inc.*, 189 W. Va. 656, 413 S.E.2d 897 (W. Va. 1991); *Alexander & Alexander, Inc. v. B. Dixon Evander & Associates, Inc.*, 88 Md. App. 672, 596 A.2d 687, 710 (Md. Special App. 1991), *cert. denied*, 605 A.2d 137 (Md. 192.)

Since the decision of *Adams*, the California Supreme Court has granted review in a number of cases involving punitive damages. *See MGW Inc. v. Fredericks Development Corp.*, 12 Cal.App.4th 244, 6 Cal.Rptr.2d 888, *review granted*, 10 Cal.Rptr.2d 85, 832 P.2d 586 (1992); *Gourley v. State Farm Mutual Automobile Ins. Co.*, slip op. 1 (1992), *review granted* July 9, 1992 (case number S014133); *Wollersheim v. Church of Scientology*, 4 Cal.App.4th 1074, 6 Cal.Rptr.2d 532, *review granted*, 10 Cal.Rptr.2d 182, 832 P.2d 898 (1992); *Hilgedick v. Koehring Finance Corp.*, 12 Cal.App. 4th 330, 8 Cal.Rptr.2d 76, *review granted*, 10 Cal.Rptr.2d 183, 832 P.2d 899 (1992).

disproportionate as to raise a presumption that it is the result of passion or prejudice.' " *Adams,* 54 Cal.3d at 118, n.9 (quoting *Neal,* 21 Cal.3d at 928).

Although a court applying the California "passion or prejudice" standard may take account of the same general considerations as the fact finder—the reprehensibility of the defendant's conduct, the relationship of the punitive award to actual damages, and the relationship of the punitive award to the defendant's financial condition—it does so *only* to determine whether the jury acted out of "passion or prejudice." *Neal,* 21 Cal.3d at 928.[4] Moreover, as just discussed, the *Neal* considerations impose no meaningful constraint.

The cursory review contemplated by the "passion or prejudice" standard, and the indefinite, illusory nature of the guidance provided by the *Neal* factors, render California's "passion or prejudice" standard of review less rigorous than the Kentucky standard of review, which this Court recently ordered the Kentucky Supreme Court to reconsider in light of *TXO. H.C. Hanson v. American National Bank & Trust Company,* 844 S.W.2d 408 (Ky. 1992), *vacated,* 61 U.S.L.W. 3669 (June 28, 1993). The standard of review that had been announced and applied by the Kentucky court in *American National Bank,* like California's standard of review, focused on whether the jury's decision was "free of passion or prejudice." 844 S.W.2d at 416.

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[4] The Alabama Supreme Court has recognized that an inquiry that is limited to a search for "passion or prejudice" does not provide adequate protection against an excessive award. " '[E]ven though a jury verdict may not be excessive because it is the result of an improperly functioning jury, it is possible for a verdict to be excessive even when it is the result of a properly functioning jury.' " *Land & Associates, Inc. v. Simmons,* 562 So.2d 140, 150 (Ala. 1989), *quoting Green Oil Co. v. Hornsby,* 539 So.2d 218, 222 (Ala. 1989).

Indeed California's *Neal* criteria for award of punitive damages are considerably less specific than the considerations mandated in Kentucky, which this Court apparently viewed as potentially insufficient in *American National Bank*. Kentucky requires a fact finder to consider the likelihood serious harm would flow from the conduct in issue, the defendant's awareness of that likelihood, the profitability of the misconduct, the duration of the misconduct, and actions by the defendant to remedy the misconduct. Ky. Rev. Stat. § 411.186 (1992). Moreover, Kentucky, unlike California, does not ask fact finders to engage in the pernicious practice of considering a defendant's wealth. *Id.*; *see* p. 25, *infra*.

The court below stated and applied California's lax "passion or prejudice" standard of review in affirming the trial court's $4.6 million punitive award.[5] Pet. App. 17a, 24a. The trial court's decision could not have survived otherwise, for it was both internally inconsistent and inconsistent with the Court of Appeal's prior ruling. The Court of Appeal's October, 1991 opinion held that an increase in punitive damages from the trial court's original $1.9 million award based on continuing bad acts by Shell was not justified because, "[i]t is equally reasonable to conclude on the basis of what was testified to that Shell no longer uses the manual or the procedures it espouses." Pet. App. 12a. Nevertheless, the trial court and the February, 1993 Court of Appeal panel upheld the trial court's increase in punitive damages on the ground that there was a "possibility Shell real estate representatives would continue to use" the manual. Pet. App. 13a-15a. On the

[5] Although the California Court of Appeal cited *Haslip* in discussing the constitutionality of the punitive award in that case, the court nevertheless did not follow the mandates of due process. As Justice O'Connor stated in *TXO*: "[T]he state courts must do more than recite the constitutional rule. They also must apply it . . . . All judges know how to mouth the correct legal rules with ironic solemnity while avoiding those rules' logical consequences." *TXO*, 61 U.S.L.W. at 4782 (O'Connor, J., dissenting).

basis of this flimsy speculation, the Court of Appeals affirmed the trial court's post-appeal $2.7 million increase in punitive damages.[6]

In short, only the most deferential review could have preserved the present award against Shell, which imposed a $2.7 million increase in punitive damages based on the thinnest evidence and internally inconsistent reasoning. California's subjective, lax standards for awarding punitive damages and its cursory appellate review of such awards have deprived Shell of its right to procedural due process. This case, like the Kentucky case, *American National Bank,* should be vacated and remanded for reconsideration in light of *TXO.*

II. THE CALIFORNIA PUNITIVE DAMAGES SYSTEM DENIED SHELL ITS RIGHT TO SUBSTANTIVE DUE PROCESS THROUGH THE AWARD AND AFFIRMANCE OF A FUNDAMENTALLY UNFAIR PUNITIVE DAMAGES AWARD

This Court has recognized that the Constitution's guarantee of fundamental fairness includes limits beyond which penalties may not go. *See TXO,* 61 U.S.L.W. at 4768 (plurality opinion); *Haslip,* 111 S.Ct. at 1045; *Seaboard Air Line Railway v. Seegers,* 207 U.S. 73, 78 (1907). A majority of this Court recognized in *TXO* that "the fact that an award is significantly larger than those in apparently similar circumstances" may be relevant to whether a punitive damages award is excessive. *TXO,* 61 U.S.L.W. at 4770 (plurality opinion); *id.* at 4776 (O'Connor, J., dissenting). An unusually large award should be subjected to constitutional scrutiny. *See*

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[6] To the extent the trial court and Court of Appeal were holding that although there was no evidence in the record of continued use, *Shell* had the burden of proving the absence of continued use, the trial court and Court of Appeal erroneously misallocated the burden of proof and thereby deprived Shell of due process. *Haslip,* 111 S. Ct. at 1046, n.11.

TXO, 61 U.S.L.W. at 4771 (although there was a "shocking" disparity between punitive and actual damages, other factors justified the award); *id.* at 4773 (Kennedy, J., concurring) (an award the size of that imposed against *TXO* might not stand if based on "vicarious liability, negligence, or strict liability"); *id.* at 4776 (O'Connor, J., dissenting) (an award of over 500 times actual damages "[a]t the very least . . . should raise a suspicious judicial eyebrow").

All objective indicia demonstrate that the award against Shell is extreme. First, the jury in this case heard all of the same evidence as the trial court (with the exception of the extremely equivocal testimony in the second trial concerning whether there was any continuing use of Shell's base lease manual). The jury awarded $235,600 in punitive damages, less than one-nineteenth the amount of the trial court's $4.6 million punitive award. This disparity within the same case raises a strong presumption that the award is arbitrary and capricious, particularly because the challenged award does not bear any "understandable relationship to compensatory damages." *Haslip*, *supra*, 111 S.Ct. at 1045.

Although the several members of this Court differed in *TXO* as to the circumstances under which an extremely large punitive award can be upheld, the exceptionally large, post-appeal increase in the punitive award against Shell cannot stand whether evaluated under the analysis of the *TXO* plurality, the concurring opinion of Justice Kennedy, or the dissent.

The plurality in *TXO* held that although an exceptionally large award may be shocking, such shock may dissipate in light of the nature of the conduct of the defendant, the potential loss to the plaintiff, and the potential gain to the defendant. *TXO*, 61 U.S.L.W. at 4771. In its final decision the trial court repeatedly emphasized that it was increasing punitive damages by $2.7 million

because it viewed Shell's business conduct in its dealings with the Nelsons as having been reprehensible. Pet. App. 30a-32a. But the trial court had reviewed *all* of the evidence with respect to such conduct when it made its initial $1.9 million punitive award. Thus, for purposes of evaluating the *post-appeal* increase, the only relevant conduct is conduct that occurrred *after* the trial court's initial $1.9 million award.

Shell's conduct after the trial court's initial award cannot justify the $2.7 million post-appeal increase. Asserting a legitimate legal argument on appeal is simply not conduct that, consistent with due process, can be punished. *See, e.g., Alabama v. Smith,* 490 U.S. 794, 798-802 (1989) ("Where the sentencing judge who presides at both trials can be expected to operate in the context of roughly the same sentencing considerations . . . any unexplained change in the sentence is therefore subject to a presumption of vindictiveness [and is invalid]."). When making the third award of punitive damages the trial court operated in precisely the same context as when making the first award of punitive damages, save for evidence that the Court of Appeal in October, 1991 held to be insufficient as a matter of law to establish continuing misconduct. Pet. App. 12a.

Moreover, although the trial court's final decision refers to Nelson Trust's potential loss and Shell's potential gain—approximately $600,000—this consideration also cannot provide support for the trial court's post-appeal $2.7 million increase in the punitive award. Pet. App. 42a. For the amount of Nelson Trust's potential loss or Shell's potential gain did not change between the trial court's initial $1.9 million award and its final $4.6 million award, but the amount of punitive damages was more than doubled. Under the analysis employed by the *TXO* plurality, the punitive award in this case is unsupportable.

Nor can the award be supported under the analysis of Justice Kennedy's concurring opinion. Justice Kennedy's conclusion that an unusually large punitive award is unsupportable if imposed on the basis of vicarious liability, negligence or strict liability disposes of the award in the instant case.[7] 61 U.S.L.W. at 4773 (Kennedy, J., concurring). One reading of the trial court's final decision would impose a (novel and incoherent) form of vicarious liability upon Shell. Although the trial court admitted there was no evidence Shell continued to use the base lease manual following the original $1.9 million punitive damages award, Shell was punished with a more than two-fold increase in the award for actions that might be taken by "persons in the field," not the actions of Shell itself. Pet. App. 13a-15a, 29a-30a.

Alternatively, the trial court's decision could be read to have imposed the additional punitive damages because Shell did not cease using the base lease manual in the manner the trial court thought appropriate. *See* Pet. App. 14a, 31a (the techniques described in the base lease manual "should not be left in a state of ambiguity"). This punishment for failure to act according to previously undefined standards of conduct (according to the trial court the wrongful conduct not only must be ceased, it must be ceased by means of a written directive) is punishment imposed based on negligence or strict liability. The post-appeal award against Shell—which the trial court based either on vicarious liability or on negligence or strict liability—is unjustified under Justice Kennedy's analysis.

The *TXO* dissent would require that a state court supply a "convincing explanation" to justify a punitive award that in light of objective indicia appears inordinately large. 61 U.S.L.W. at 4776 ("[A]bsent a convincing ex-

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[7] Whatever Nelson Trust may say as to the nature of Shell's business conduct prior to the trial court's first award of punitive damages, such conduct cannot justify the $2.7 million *increase* in punitive damages after Shell's partially successful appeal.

planation this . . . award—over 500 times actual damages —surely must cross" the constitutional line.) As discussed, the Court of Appeals engaged in only a cursory review before affirming the trial court's $2.7 million post-appeal increase in punitive damages, and the courts below have offered only unjustified explanations for the increase.

The *TXO* plurality opinion, Justice Kennedy's concurrence, and the dissent all express particular concern about the tendency of both juries and judges to impose inordinate punitive awards on wealthy, out-of-state companies. As Justice O'Connor wrote, "the temptation to transfer wealth from out-of-state corporate defendants to in-state plaintiffs can be quite strong." *Id.* at 4780 (O'Connor, J., dissenting). Shell, of course, is just such a wealthy out-of-state company. "Given the absence of another plausible rationale" for the trial court's "monumentally large" post-appeal increase in punitive damages it seems that the trial court may well have been "influenced unduly by" Shell's "out-of-state status and its large resources." *Id.* at 4780 (O'Connor, J., dissenting).

The trial court specifically referred to Shell's wealth at length in assessing the post-appeal $2.7 million increase, stating: "Another factor considered in assessing punitive damages against Shell is its wealth. A financial 'slap on the wrist' of a wrongdoer in [sic] tantamount for [sic] no penalty at all." Pet. App. 32a. The trial court here was influenced unduly by Shell's wealth. Shell's wealth does not provide a reasoned basis for the post-appeal increase in punitive damages.

In short, under *TXO* the trial court's $4.6 million punitive award is unsupportable. This Court should vacate the trial court's judgment and remand this case for reconsideration in light of *TXO*.

III. CALIFORNIA'S PROCEDURES FOR CALCULATING A RATIO OF PUNITIVE TO ACTUAL DAMAGES WHEN ATTORNEY'S FEES HAVE BEEN AWARDED ARE ARBITRARY AND CAPRICIOUS IN LIGHT OF CALIFORNIA'S ARTICULATED PURPOSES FOR AWARDING PUNITIVE DAMAGES

A state's procedures for determining a punitive damages award must assure "that punitive damages are reasonable in their amount and *rational in light of their purpose* to punish what has occurred and to deter its repetition." *Haslip,* 111 S. Ct. at 1044-45 (emphasis added). As the dissenting opinion in *TXO* states, "due process does not simply require that a particular result be substantially acceptable; it also requires that it be reached on the basis of permissible considerations." *TXO,* 61 U.S.L.W. at 4778 (O'Connor, J., dissenting). But the California courts' consideration in this case of the appropriate ratio of punitive to actual damages was arbitrary and irrational in light of California's articulated purposes for awarding punitive damages. Nelson Trust's damages in this case consisted almost entirely of attorney's fees. Yet no procedure provided any means for rationally relating the size of the punitive damages award to Nelson Trust's actual damages in light of the fact Nelson Trust already had been awarded the litigation expenses incurred in vindicating its rights.[8]

A simple example illustrates the error below. Suppose in a tort action, case 1, the plaintiff is awarded $10,000 in actual damages and the court finds that a ratio of punitive to actual damages of two-to-one is appropriate, awarding $20,000 in punitive damages. In a similar tort action, case 2, the plaintiff is awarded the same $10,000 in actual damages plus an additional $20,000 in attorney's fees. Assuming all else to be equal (the defendants' con-

[8] Although in *TXO* the "compensatory" damages consisted of respondent's cost of defending against petitioner's declaratory judgment action, this impropriety was neither raised by the parties nor addressed by this Court. *TXO,* 61 U.S.L.W. at 4768.

duct, etc.), the plaintiff in the second case surely is *not* entitled to a $60,000 punitive damages award based on a two-to-one ratio of punitive damages to actual damages plus attorney's fees.

The reason for considering the ratio of punitive to actual damages in California as in most other states is to provide some measure of proportionality between the punitive award and the actual harm done to the plaintiff. *See, e.g., Adams,* 54 Cal.3d at 109-10; *Neal,* 21 Cal.3d at 928 ("in general, even an act of considerable reprehensibility will not be seen to justify a proportionately high amount of punitive damages if the actual harm suffered thereby is small.") In the hypothetical example, the harm is not greater in the second case than in the first. To the contrary, in the second case the attorney's fees award makes the victim whole for the cost of vindicating his rights even before the punitive damages award. If anything, case 2 justifies a *lesser* punitive damages award than case 1. The California courts' consideration of the punitive to compensatory damages ratio here, entirely divorced from and in conflict with the articulated purposes of punitive damages in California, violated due process.

In this case, the actual damages awarded to Nelson Trust consisted of a very modest award of $6,133 in lost interest income. Pet. App. 56a. Thus the ratio of punitive to actual damages is $4.6 million to $6,133 or approximately 750 to 1. Nelson Trust also was awarded attorney's fees in the amount of $275,208. Pet. App. 56a. It is only by adding the attorney's fees award to actual damages that the Court of Appeal obtained a ratio of punitive damages of 17 to 1.

No procedure on appeal checked whether the jury's award was consistent with California's purposes for awarding punitive damages or its articulated criteria for determining the amount of an award. The court below considered whether the award was "excessive" by con-

sidering the ratio of punitive to actual damages, the actual damages consisting almost entirely of attorney's fees. Where damages consist solely or partly of attorney's fees, consideration of a ratio of punitive to all other damages does not assure that the punitive damages bear a rational relationship to the extent of harm to the plaintiff. *See Amica Mutual Ins. Co. v. Schettler,* 768 P.2d 950, 967 (Utah Ct. App. 1989) (attorney's fees "go on neither side of the scale when determining whether the amount of punitive damages awarded 'bear[s] a reasonable relation' to the amount of general damages"); *Byler v. Garcia,* 685 S.W.2d 116, 120 (Tex. Ct. App. 1985) (trial court properly did not include attorney's fees award in its consideration of punitive damages).

When a state considers the amount of harm to the plaintiff in determining the appropriate size of a punitive damages award, the state's procedures for trial or appellate review of excessiveness also must take into account whether or not the plaintiff already has been compensated for the "harm" of incurring litigation expense to vindicate his rights. In the hypothetical situation described above, the plaintiffs in cases 1 and 2 suffered the same amount of harm. In case 2, before the award of punitive damages, the plaintiff was compensated for the harm done by the defendant's wrongful acts *and* for the cost of obtaining reimbursement for that harm (the attorney's fees award). The state's procedures for measuring the excessiveness of a punitive damages award may not irrationally measure "harm" to the plaintiff in case 1 without reference to the cost of vindicating rights but measure "harm" in case 2 as *including* the costs of bringing and prosecuting the lawsuit.

Moreover, California law is clear that punitive damages cannot be increased on a dollar for dollar basis to compensate a plaintiff for attorney's fees. The plaintiff's costs of litigation are *not* to be considered in awarding punitive damages under California law. *Viner v. Un-*

trecht, 26 Cal.2d 261, 158 P.2d 3 (1946) (punitive damages cannot include attorney's fees).

Because California declines to allow a jury or court to take into account the costs of litigation in awarding punitive damages, it has made a judgment that punitive damages should not be higher to compensate the plaintiff for litigation expenses. If a trial or appellate court, however, calculates a ratio of punitive to compensatory damages for purposes of determining whether the award is excessive and *includes* an attorney's fees award in the denominator of the ratio without any other adjustment, the court has refused to give the defendant the benefit of the criteria the state purports to apply. Under this procedure for calculating the ratio, as the hypothetical described above demonstrates, a one dollar increase in attorney's fees will justify a punitive award that is several dollars higher. Though the state purports to apply a system in which attorney's fees are not included within punitive damages, it in fact is increasing punitive damages *geometrically* solely based on attorney's fees.

Moreover basing a ratio on the amount of attorney's fees incurred by the plaintiff in many cases will lead to absurd results. A defendant has no control over the energy and resources a plaintiff chooses to bring to bear in litigation. If the attorney's fees in this case had been $1 million, the line of reasoning of the courts below would have justified a punitive damages award of approximately $17 million. This approach becomes even more absurd, when, as is sometimes the case, plaintiff's counsel's fee award already is based on a multiplier.

Thus, the "excessiveness" calculus engaged in by the California courts in this case did not assure adherence to the state's criteria for determining punitive damages. Consideration of an appropriate ratio of punitive to compensatory damages must assure consistency with the criteria chosen by the state for determining the amount of punitive damages. The courts below, by contrast, utterly

ignored the state's rationales for awarding punitive damages by failing to recognize that the attorney's fees award itself reduced the need for a punitive damages award, and instead increasing punitive damages geometrically based on attorney's fees.

Just as a state cannot constitutionally deprive a defendant of property without some meaningful criteria for determining the amount of an award, it cannot constitutionally articulate valid criteria but refuse to apply them. This Court has recognized that "concrete problems of constitutional dimension" under the Due Process Clause sometimes may emerge through arbitrary and discriminatory enforcement of state law. *Village of Hoffman Estates v. Flipside, Hoffman Estates, Inc.*, 455 U.S. 489, 504 (1982) (citing *Joseph E. Seagram & Sons, Inc. v. Hostetter*, 384 U.S. 35, 52 (1966)). Such a problem has emerged here.

The state of California determined that punitive damages should *not* provide compensation to the plaintiff for the costs of the lawsuit. It also determined that punitive damages should be proportional to the harm to the plaintiff. But the California courts' purported application of these criteria in fact conflicts with them. The California courts did not merely compensate Nelson Trust for the costs of bringing suit through the punitive award; through the multiplier effect of the ratio they provided Nelson Trust many times such costs. Further, the courts failed to lower the punitive damages ratio in recognition of the fact that the award of attorney's fees already had served to reduce the harmful effects of the defendant's conduct.

Whatever guidance and predictability California's criteria for calculating punitive damages may have had in and of themselves, they lost those neutral qualities in the California courts' interpretation and application of those criteria in this case. California's purported test for when a punitive damages award is "excessive" violates the Due Process Clause.

CONCLUSION

For the foregoing reasons this Court should grant Shell's Petition for Certiorari. In the alternative this Court should grant the Petition, vacate the judgment below, and remand this case for reconsideration in light of *TXO*.

Respectfully submitted,

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July 15, 1993

APPENDICES

APPENDIX A

Second Appellate District, Division One, No. B067801
S032118

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA
IN BANK

CHARLOTTE NELSON, *et al.*,
Respondents,

v.

SHELL OIL COMPANY,
Appellant.

Appellant's petition for review DENIED.

[Filed May 26, 1993]

/s/ Lucas
Chief Justice

APPENDIX B

IN THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA
SECOND APPELLATE DISTRICT
DIVISION ONE

B067801
(Super. Ct. No. C552457)

CHARLOTTE NELSON, *et al.*,
Cross-complainants and Respondents.

v.

SHELL OIL COMPANY,
Cross-defendant and Appellant.

[Filed Feb. 26, 1993]

APPEAL from a judgment of the Superior Court of Los Angeles County, Arthur Baldonado, Judge. Affirmed.

Munger, Tolles & Olson, Ronald L. Olson, Carolyn B. Kuhl, Patrick D. Harvill, Schreiber & Horn, Inc., Gregory Horn, Edwin C. Schreiber and Mark Schreiber for Cross-defendant and Appellant.

Hobart & Heeringa, G. Dana Hobart, Kent Heeringa and Donald B. Caffray for Cross-complainants and Respondents.

INTRODUCTION

Appellant Shell Oil Company appeals from a judgment fixing punitive damages following remand by the appellate court. It was the second retrial on the issue of damages following the original trial at which liability was determined.

STATEMENT OF FACTS

The property at issue in this case, originated as an eminent domain action filed by Caltrans against appellant Shell Oil Company (Shell) and respondents, the Nelsons, located at 5548 West Imperial Highway, has been owned by members of the Nelson family since 1942. Shell began leasing the property in 1950 and operated a service station on it. (*Shell Oil Co.* v. *Nelson* (May 24, 1989) B030269, typed opn. pp. 2-3 (*Nelson I*).)

On March 16, 1960, Shell entered into a 15-year lease agreement for the property with Edward and Charlotte Nelson. The lease ran from May 1, 1961 through May 31, 1976 and included a 10-year option. Under the lease, monthly payments were $1135—$806.66 in rent and $328.40 to repay a reconstruction loan from the Nelsons to Shell.[1] If the option were exercised, monthly rent would be $910. The lease did not provide for rent adjustment to respond to inflation, it included a 90-day termination clause in Shell's favor, required the Nelsons to pay up to $2400 in property taxes on the property annually and required the Nelsons to pay for fire insurance. (*Nelson I, supra,* typed opn. p. 3.)

In March 1975, a representative of Caltrans contacted Dale A. Lewis (Lewis), a Shell real estate representative. Due to its plans to widen Sepulveda Boulevard and construct the Century Freeway, Caltrans purchased a property located at Imperial Highway and Sepulveda Boulevard, on which Shell had a service station. Caltrans

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[1] Although $806.66 and $328.40 actually add up to $1135.06, these are the figures given in *Nelson I*.

paid Shell $11,500 for its fixtures on the property. (*Nelson I, supra,* typed opn. pp. 3-4.)

From December 1975 through March 1976, Lewis unsuccessfully attempted to negotiate three five-year options to the Nelson lease, which was soon to expire. Lewis offered the Nelsons a $6000 bonus for the extensions; the Nelsons rejected this offer and proposed that Shell pay all property taxes on the property and that the rental for the property be based on the appraised value of the property at the time the options were exercised. Shell rejected this proposal and abandoned the negotiations on Lewis' recommendation. (*Nelson I, Supra,* typed opn. p. 4.)

Shell exercised its 10-year option to renew the lease in April 1976. Although, under the option, monthly rental payments were to decrease to $910, Shell continued to pay the Nelsons $1135 per month. The overpayments continued for more than two years and reached $5625. (*Nelson I, supra,* typed opn. pp. 4-5.)

Lewis was informed of the overpayments in May 1978, and he immediately notified the Nelsons; Edward Nelson responded that it would be a hardship for him to repay the $5625. Lewis met with Edward and Charlotte Nelson at their Leisure World apartment in June 1978. Lewis spoke with Mrs. Nelson about Mr. Nelson's failing health: Mr. Nelson, who would turn 80 the following week, had recently been having heart trouble and losing weight; he had been to his doctor's office that week and to the hospital emergency room suffering from dizziness and chest pain. (*Nelson I, supra,* typed opn. pp. 5-6.)

Lewis then met with Mr. Nelson; they spoke for 30 minutes to an hour. While they were talking, Mrs. Nelson remained nearby and listened to the discussion. As stated in *Nelson I*: "Mrs. Nelson heard Lewis explain to Mr. Nelson that he had two choices—either pay back the $5,625 overpayment or agree to an additional 15 year lease on the lot in exchange for Shell forgiving the

indebtedness. Mr. Nelson proposed that a 'cost of living' rental increase be included in the lease. Lewis unequivocally rejected this idea. Lewis stated that Shell was very happy with the station location, looked forward to many years of business there, and had long-range plans for it. He also reminded Mr. Nelson that the monthly rental check would be comforting to Mrs. Nelson and offer financial security for her should anything happen to him. . . . Mrs. Nelson felt Lewis created an atmosphere of urgency during this meeting. No mention was made of the Century Freeway or possible condemnation of the property by Caltrans. Mrs. Nelson had no information at that time about any possible effect the Century Freeway might have on the property. By the time Leiws left, Mr. Nelson had agreed to the three five-year options to extend the lease to 2001. All other lease terms remained the same." (*Nelson I, supra,* typed opn. pp. 6-7, fn. omitted.)

The Nelsons signed an agreement amending the lease on June 8, 1978. It provided for increased rent in 2001 of $1200 per month; otherwise, the lease terms would be the same. Mrs. Nelson signed the agreement "because she trusted her husband's judgment and realized that in order to repay the $5625 they would have had to borrow or sell stock, thereby reducing their income." (*Nelson I, supra,* typed opn. p. 7.) Shell signed the agreement on June 20. (*Ibid.*)

At the time Lewis negotiated the lease extension with the Nelsons, he knew construction of the Century Freeway still was a possibility and the state still was buying property in the freeway corridor. (*Nelson I, supra,* typed opn. p. 7, fn. 7.) He also knew that if the state condemned property in the freeway corridor it would compensate the owners of the property, "and that a lessee who had a right into the future beyond the period of condemnation was entitled to make a claim for a certain percentage of the overall state payment for the property.

He was also aware that options counted in determining the length of the lease, and that the lower the rent the more Shell's claim in condemnation was worth." (*Id.* at p. 8.)

Among the training and policy manuals available to Shell real estate representatives was the Shell Base Lease Manual. During their training seminars, real estate representatives were instructed to follow the procedures outlined in this manual. Shell also provided a Condemnation Manual, which instructed real estate representatives to keep abreast of further developments upon learning of a possible condemnation. (*Nelson I, supra,* typed opn. pp. 8-9.)

The base lease manual offered tips on how to deal with various issues and persuade owners to accept lease provisions favorable to Shell. "Among the tips described in the Base Lease Manual, were suggestions on how to minimize a lease feature by hurrying along, joking, or grouping together and dismissing as unimportant the desired feature; [and] on how to convince an owner to pay his or her own property taxes . . . . The Manual emphasizes the importance of timing in renewal negotiations; the advantages of placing the owner in a 'defensive position' and in a 'frustrated position'; and directs the real estate representatives to 'be familiar with all instructions relating to condemnations.' It further suggests that when Shell wants to secure a long term lease from 'an owner who is middle-aged or slightly beyond,' the representative should tell the owner that 'a long lease gives . . . security of income for . . . old age, . . . [.] It suggests reminding an owner that, 'After a man dies, his family is always better off if it has a steady income. . . . It is very difficult to plan an estate on a short-term lease. Widows and children need the protection afforded by the experience and ability of a successful business man. That protection can be extended by an owner through the use of [a] long-term lease.' " (*Nelson I, supra,* typed opn. pp. 8-9.)

Edward Nelson died in mid-1979. (*Nelson I, supra,* typed opn. p. 6, fn. 6.) In October 1979, a federal court dissolved the injunction which prevented construction of the Century Freeway. In March 1983, Charlotte Nelson learned after receiving a letter from Caltrans that the Imperial Highway property was to be condemned for construction of the Century Freeway. In November 1984, she learned Shell was making a claim on the condemnation proceeds. Shell sought two-thirds of the condemnation award. According to its expert, the value of its leasehold interest was $620,000; this valuation was based on his opinion fair rental value of the property was $7900 per month. (*Id.* at pp. 10-11.)

This case first was tried in 1987. As a result of that trial, the agreement providing the three five-year options to extend the lease was rescinded based on fraud on the part of Shell, which, "via its real estate representative who acted upon the offensively manipulative advice printed in Shell's base lease manual, . . . acquired the three five-year options on the . . . property, knowing that Caltrans' Century Freeway project would require eminent domain acquisition of this property. This occurred when the late Edward Nelson was 80 years old and in severe ill health. When Caltrans filed its eminent domain action, Shell claimed the lion's share of the award . . . ." (*Nelson* v. *Shell Oil Company* (Oct. 21, 1991) B055153, typed opn. p. 2, fn. 1 (*Nelson II*).)

As a result of Shell's fraudulent actions, financial losses were sustained by the Nelson Trust, which at some point in time acquired ownership or control over the Imperial Highway property. First, while litigation over apportionment of the condemnation award was ongoing, disbursement of $624,000 of the award was blocked. The Nelson Trust's loss of use of those funds resulted in financial losses. (*Nelson II, supra,* typed opn. pp. 16-17.) Additionally, the Nelson Trust was required to make expenditures for attorney's fees in litigation to defend against

Shell's claims in the eminent domain proceedings and to ensure the state would not release to Shell any part of the condemnation award to which it was not entitled. (*Id.* at pp. 14-15.)

After the first trial in this case in 1987, but before it was retried on the issue of damages, the Nelson Trust subpoenaed from Shell " 'any and all writings or documents wherein Shell either modified, withdrew, repudiated or otherwise prevented or discouraged the continued use of its base lease manual or any part thereof . . . .' No documents were produced in response to that subpoena, and counsel for Shell stipulated that no such documents exist." (*Nelson II, supra,* typed opn. p. 24.) Shell's real estate manager testified that since 1987 "he had not prepared any communication discussing or modifying the use of the manual, nor had he seen such a document. [However, h]e also testified that since 1987 he had not directed anyone to use the manual and was not aware if one was available in his office." (*Ibid.*)

PROCEDURAL BACKGROUND

The action by Caltrans against Shell and the Nelsons was filed on June 18, 1985. The Nelsons then filed a cross-complaint against Shell. Pursuant to an interlocutory judgment filed October 27, 1986, the state agreed to pay $975,000 to Shell and the Nelsons; apportionment of this award between the parties was to be decided at trial. (*Nelson I, supra,* typed opn. p. 11.)

The Nelsons' causes of action against Shell for fraud, constructive fraud and intentional infliction of emotional distress were tried to a jury. The jury returned special verdicts in favor of the Nelsons for $154,150 in compensatory damages and $235,600 in punitive damages. The Nelsons' cause of action for rescission was tried by the court, which granted the Nelsons rescission and awarded them $1,900,000 in punitive damages, less certain deductions. The trial court also granted the Nelsons

a new trial on the issue of damages on their fraud cause of action, but the Nelsons later elected the remedy of rescission and did not pursue the new trial. Judgment was entered September 18, 1987. (*Nelson I, supra,* typed opn. pp. 12-13.)

Shell appealed the judgment. In *Nelson I, supra,* filed May 24, 1989, Division Four of this court affirmed the rescission but reversed the award of punitive damages on the ground no compensatory damages had been proven or awarded. (Typed opn. pp. 21-22.)

The parties returned to the trial court, where the Nelsons moved for a new trial on the issue of damages; the motion was granted. Shell petitioned Division Four of this court for a writ of mandate/prohibition, seeking to reverse the new trial order; the petition was denied for failure to show facts justifying extraordinary relief. Shell then appealed the order granting a new trial; Division Four dismissed the appeal as being from a nonappealable order. Following the dismissal, a new trial was held. The trial court awarded the Nelsons $352,242 in compensatory damages and $6,295,000 in punitive damages. (*Nelson II, supra,* typed opn. pp. 2-3.)

Shell appealed the judgment. In *Nelson II, supra,* filed October 21, 1991, Division Four of this court modified the compensatory damage award and affirmed it as modified. It also struck the punitive damage award as excessive, adding: "It appearing that all of the evidence necessary to a determination of the issue of punitive damages is before the court, we see no necessity for a further trial. It only remains for the trial court to arrive at an amount of punitive damages supported by the evidence. The matter is remanded for the trial court to assess and award punitive damages consistent with the views expressed in this opinion." (Typed opn. pp. 26-27.)

Shell petitioned the court for a rehearing; the petition was denied. Shell then petitioned the Supreme Court for

review; this petition also was denied. The case was then remanded to the trial court, which reconsidered the evidence and awarded the Nelsons $268,891 in compensatory damages and $4,600,000 in punitive damages.

CONTENTIONS

I

Appellants contends the trial court's award of $4.6 million in punitive damages directly contradicts the holding of a previous opinion of this court and therefore must be reversed.

II

Appellant further contends the trial court's punitive damages award, violates the standards for assessing punitive damages under California law.

III

Appellant asserts the trial court's punitive damages award also violates rights protected by the United States and California constitutions.

DISCUSSION

I

Appellant contends the trial court's award of $4.6 million in punitive damages directly contradicts the holding of a previous opinion of this court and therefore must be reversed. We disagree.

Under the law of the case doctrine, where an appellate court in deciding an appeal " 'states in its opinion a principle or rule of law necessary to the decision, that principle or rule of law becomes the law of the case and must be adhered to throughout its subsequent progress, both in the lower court and upon subsequent appeal. . . .' " (*People* v. *Shuey* (1975) 13 Cal.3d 835, 841;

accord, *Clemente* v. *State of California* (1985) 40 Cal.3d 202, 211.) Thus, if, following a reversal on appeal, a case is again decided and appealed, the appellate court " 'generally will not inquire into the merits of said first decision, but will regard it as the law of the case.' " (*Shuey, supra,* at p. 841; accord, *Clemente, supra,* at pp. 211-212.) However, the doctrine will only be applied where the point of law involved was necessary to the prior decision, actually presented to and determined by the court, and application of the doctrine will not result in an unjust decision. (*Shuey, supra,* at p. 842.)

While the law of the case doctrine is concerned with issues of law rather than fact (*People* v. *Shuey, supra,* 13 Cal.3d at p. 842), it may affect factual determinations. Where an appellate court makes a determination on the sufficiency of the evidence to sustain a judgment, that determination is the law of the case. (*Ibid.*; 9 Witkin, Cal. Procedure (3d ed. 1985) Appeal, § 748, p. 716.) If there is no substantial difference in the evidence on retrial, the decision on the prior appeal as to its sufficiency is binding on the trial court and appellate court on a subsequent appeal. (*Id.*, §§ 737, 748, pp. 705, 716-717.)

In *Nelson I, supra,* the trial court's award of $1,900,000 in punitive damages was reversed on the ground no compensatory damages had been proven or awarded. (Typed opn. pp. 21-22.) Following retrial on the issue of damages, the trial court awarded the Nelsons $352,242 in compensatory damages and $6,295,000 in punitive damages. On appeal from that judgment, Shell contended the trial court erred in increasing the punitive damages award based on evidence of Shell's use of the base lease manual after the original trial in this case in 1987, and the evidence was insufficient to support the increased punitive damages award. (*Nelson II, supra,* typed opn. pp. 23-24.)

The appellate court held the trial court properly considered evidence of Shell's actions between 1987 and the

retrial; it was relevant to the issue of malice. (*Nelson II, supra,* typed opn. pp. 23-24.) In determining whether the evidence was sufficient to support the increased punitive damages award, the court summarized the evidence on the issue as follows: After the first trial in this case in 1987, but before the retrial on the issue of damages, the Nelson Trust subpoenaed from Shell "'any and all writings or documents wherein Shell either modified, withdrew, repudiated or otherwise prevented or discouraged the continued use of its base lease manual or any part thereof. . . .' No documents were produced in response to that subpoena, and counsel for Shell stipulated that no such documents exist." (*Id.* at p. 24.) Shell's real estate manager testified that since 1987 "he had not prepared any communication discussing or modifying the use of the manual, nor had he seen such a document. [However, h]e also testified that since 1987 he had not directed anyone to use the manual and was not aware if one was available in his office." (*Ibid.*)

According to the appellate court, "[t]he trial court interpreted the evidence in the second trial as establishing that Shell was continuing to utilize the 'manipulative techniques advanced in the manual.' However, this conclusion is simply not supported by the evidence. It is equally reasonable to conclude on the basis of what was testified to that Shell no longer uses the manual or the procedures it espouses. The Nelson Trust did not meet its burden on this issue. We conclude that the court abused its discretion in assessing punitive damages of $6.295 million." (*Nelson II, supra,* typed opn. p. 25.) The court struck the punitive damages award as excessive. Since it appeared all the evidence necessary to determine the issue of punitive damages was before the trial court, the court saw no necessity for a retrial but remanded the case for the trial court to "arrive at an amount of punitive damages supported by the evidence." (*Id.* at pp. 26-27.)

On remand, no further trial proceedings were held and no additional evidence was introduced. Thus, the law of the case doctrine applies to the appellate court's determination in *Nelson II* as to the sufficiency of the evidence to support the increased punitive damages award. (*People* v. *Shuey, supra,* 13 Cal.3d at p. 842; 9 Witkin, *op. cit. supra,* § 748, p. 716.) It is the law of the case that the evidence presented does not establish that "Shell was continuing to utilize the 'manipulative techniques advanced in the [base lease] manual.'" (*Nelson II, supra,* typed opn. p. 25.)

The trial court on remand again awarded punitive damages in excess of the $1.9 million awarded after the first trial in 1987—this time $4.6 millon. In its statement of decision, the trial court reviewed the evidence, then explained the basis of this award: "It is clear that following the first trial Shell undertook no official action to withdraw, modify or rescind the techniques they were using when negotiating service station leases. If there was to be some change in these practices it was not evidenced. It can be inferred from [the real estate manager's] testimony that no such change had ever been thought of.

"This is not to conclude that Shell did or did not continue to follow the principles advocated in the manual following the second trial. However, an inference may be fairly drawn that in the absence of any written directives Shell undertook no meaningful or effective efforts to communicate any rescission of its prior policy as set forth in the manual. It is also reasonable to infer that in the absence of any written modification the persons in the field, who were negotiating service station leases, had not been clearly told to halt their use of methods of fraud advocated in the manual.

"[The real estate manager] testified there are older and younger real estate representatives. At a minimum it would be expected that if the punitive damage assessment

from the first trial were to have any effect at all, the older representatives who were trained by using the base lease manual would be directed to avoid or discontinue using the fraudulent methods taught in the manual. Without some form of unequivocal notification that the old ways were to be discontinued, how can any objective observer be convinced there has been a change in practice? Some effort following the first trial to withdraw or recall the base lease manuals would be reasonably expected if the first punitive damage award was seen as anything beyond a mere nuisance."

The trial court was of the opinion the manipulative techniques recommended in the base lease manual "should not be left in a state of ambiguity. By not rescinding such methods promptly and clearly Shell has at a minimum left the continued use of these methods up to the individual choice of field personnel, many of whom were trained to follow these techniques. It is obvious that the first assessment of punitive damages has been insignificant considering that one of the purposes of punitive damages is to deter future conduct of a similar nature. It is clear that Shell has not accepted that such conduct is an unacceptable business practice."

The trial court then reviewed the conduct by Shell which supported the imposition of an award of punitive damages in the first place, Shell's wealth, and the ratio between actual and punitive damages. After considering the evidence and the pertinent factors, the trial court fixed the punitive damages award at $4,600,000.

While the trial court obviously was of the opinion "Shell was continuing to utilize the 'manipulative techniques advanced in the [base lease] manual' " (*Nelson II, supra,* typed opn. p. 25), it does not appear this was the basis of its punitive damages award. In fact, the court specifically stated it was not concluding "that Shell did or did not continue to follow the principles advocated in the manual."

Rather, the basis of the trial court's decision was the fact that "Shell undertook no official action to withdraw, modify or rescind the techniques" advanced in the manual. This left open the possibility Shell real estate representatives would continue to use these manipulative and fraudulent techniques condemned in the first trial. It was obvious to the trial court that the $1.9 million assessment of punitive damages at the first trial was not significant enough to deter future similar conduct, and Shell had not accepted that such conduct was an unacceptable business practice. For these reasons, it awarded $4.6 million in punitive damages, more than that awarded at the first trial.

Since the basis for the trial court's determination was different, the determination does not violate the law of the case doctrine; the particular issue decided by the trial court on remand is not the same one decided by it on the previous retrial and reviewed by the appellate court. (*People* v. *Shuey, supra,* 13 Cal.3d at p. 842; see also *Searle* v. *Allstate Life Ins. Co.* (1985) 38 Cal.3d 425, 435.) Thus, it need not be reversed on that ground.

II

Appellant further contends the trial court's punitive damages award violates the standards for assessing punitive damages under California law. Again, we disagree.

Shell first claims the award violates the applicable standards because the trial court placed the burden of proof on it to show an increase in punitive damages was not appropriate rather than placing the burden of proof on the Nelsons to show an increase was appropriate. The trial court did this by requiring Shell to prove it no longer was using the base lease manual after the first trial in 1987, after the Nelsons failed to prove it continued to use the manual on retrial.

As a general rule, a party asserting a claim for relief has the burden of proving the existence or nonexistence of every fact necessary to support that claim. (Evid.

Code, § 500; *Adams* v. *Murakami* (1991) 54 Cal.3d 105, 119.) In the case of punitive damages, fundamental fairness requires that the party seeking such damages bear the burden of proving the appropriateness both of their imposition and of their amount. (*Id.* at pp. 119-120.) "It is not too much to ask of a [party] seeking such a windfall to require that he or she introduce evidence that will allow a [trier of fact] and a reviewing court to determine whether the amount of the award is appropriate and, in particular, whether it is excessive in light of the central goal of deterrence." (*Id.* at p. 120.)

A review of the trial court's statement of decision reveals that the trial court did, in fact, properly place the burden of proof on the Nelsons. It indicated the Nelsons subpoenaed from Shell any official documents which would show Shell had discontinued use of the base lease manual; Shell produced no such documents and stipulated that none existed. The trial court also indicated the Nelsons produced a witness, Shell's real estate manager, who "testified that he had not prepared any document discussing or modifying the use of the manual. Nor was he aware of any official notice from Shell Oil Company directed to Shell employees in California or elsewhere modifying or curtailing the practices advanced in the base lease manual." The Nelsons proved, to the trial court's satisfaction, "that following the first trial Shell undertook no official action to withdraw, modify or rescind the techniques they were using when negotiating service station leases. If there was to be some change in these practices it was not evidenced. It can be inferred from [the real estate manager's] testimony that no such change had ever been thought of." From the absence of any evidence Shell took any steps to change the policies in the base lease manual which had been condemned in the first trial, it may be inferred Shell took no such steps. (Cf. *Greening* v. *General Air-Conditioning Corp.* (1965) 233 Cal.App.2d 545, 550.)

If any burden was placed on Shell, it was the burden of actually taking such steps so that the Nelsons could find some evidence they had been taken. But it was not the burden of proving in court it had taken the steps; the Nelsons proved it had not.

Shell next claims the punitive damages award in excess of that awarded after the first trial was the result of passion and prejudice. Specifically, there is no evidence to support the award, so it must have been based solely on the trial court's determination to punish Shell for pursuing its right of appeal.

An award of punitive damages may be upheld on appeal only where supported by the evidence and must be reversed where it is unsupported and appears to have been the result of passion and prejudice. (*Neal* v. *Farmers Ins. Exchange* (1978) 21 Cal.3d 910, 927-928; accord, *Adams* v. *Murakami, supra,* 54 Cal.3d at pp. 109-110.) In determining whether the award is supported by the evidence or may be presumed to be the result of passion and prejudice, certain factors are to be considered. These factors relate to the purpose of punitive damages, which is to punish past wrongdoing and deter future wrongdoing. (*Id.* at p. 110; *Neal, supra,* at p. 928.)

The first factor is the nature of the particular acts to be punished in light of the whole record; the more reprehensible the acts, the greater the appropriate punishment. (*Neal* v. *Farmers Ins. Exchange, supra,* 21 Cal.3d at p. 928.) Another factor is the amount of compensatory damages; the punishment must bear a reasonable relationship to the amount of harm actually suffered. (*Ibid.*) A third factor is the wealth of the party against whom punitive damages are awarded; the award must be significant enought to cause the party discomfort if the function of deterrence is to be served. (*Ibid.*)

It is Shell's position that evidence of the first factor is lacking, based on the holding of *Nelson II* that there is insufficient evidence to support a conclusion Shell continued to use the base lease manual. Thus, in Shell's view, there is no evidence of continuing bad acts justifying the imposition of a punitive damages award greater than that which was made after the first trial and held in *Nelson II* to be supported by the evidence and to bear a reasonable relationship to compensatory damages.[2]

However, the trial court found continuing bad acts in Shell's failure to take any steps to ensure the base lease manual and the manipulative policies therein—found to be fraudulent after the first trial—would no longer be used. This left open the possibility Shell's real estate representatives would continue to act in accordance with these policies. The trial court justified its imposition of the higher punitive damages award as follows: "It is obvious that the first assessment of punitive damages has been insignificant considering that one of the purposes of punitive damages is to deter future conduct of a similar nature. It is clear that Shell has not accepted that such conduct is an unacceptable business practice. In assessing punitive damages the court is mindful of certain consideration[s]. The more corrupt and cruel the conduct the greater the amount [of punitive damages] should be. Shell's conduct is at the outer limits of intolerable business practice. The court also considers the public interest and the need to prevent this type of conduct." The trial court considered $4.6 million in punitive damages to be "the minimal amount that will deter future conduct and fairly and justly punish outrageous and fraudulent conduct."

The record contains evidence which supports the imposition of an increased punitive damages award based on

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[2] Shell only discusses the first two factors. It makes no claim the punitive damages award is excessive baed on its wealth.

continuing bad acts. Additionally, the trial court properly considered the nature of those acts and the goal of deterrence in making the award. Since the original award failed to impel Shell to take any action to ensure its past fraudulent acts would not be repeated, the trial court could "reasonably conclude its [increased] award of punitive damages was necessary in order to get [Shell's] attention." (*Moore* v. *American United Life Ins. Co.* (1984) 150 Cal.App.3d 610, 638.)

As to Shell's claim that the increase in the punitive damages award was to punish Shell for pursuing its right of appeal, there is no evidence to support this claim. Shell bases its claim solely on its perceived lack of evidence of continuing bad acts to support the increased punitive damages award. Since there is such evidence, Shell's claim is without merit.

Shell next argues the $4.6 million punitive damages award is unsupported by the second *Neal* factor, in that it bears no reasonable relationship to the compensatory damages award of $268,891. Specifically, the ratio between the two is approximately 17 to 1, which crosses the line of reasonableness.

In support of its argument, Shell relies on *Pacific Mut. Life Ins. Co.* v. *Haslip* (1991) —— U.S. —— [113 L.Ed.2d 1]. In *Haslip*, the ratio between punitive and compensatory damages was approximately 4 to 1, and punitive damages were 200 times the respondent's out-of-pocket expenses. The Supreme Court noted that the monetary comparisons were wide and may have been "close to the line," but it concluded the punitive damages award did "not cross the line into the area of constitutional impropriety." (At p. 23, fn. omitted.)

Shell also cites *Las Palmas Associates* v. *Las Palmas Center Associates* (1991) 235 Cal.App.3d 1220, 1255, in which punitive damages were reduced to a level that

was 7.9 times greater than compensatory damages. However, inasmuch as the reason punitive damages were reduced was that compensatory damages had been reduced, and the original punitive and compensatory damages awards bore a ratio of approximately 7.9 to 1, *Las Palmas Associates* is not instructive.

The United States Supreme Court in *Haslip* did not purport to set the line of constitutional impropriety in terms of the relationship between punitive and compensatory damages. Obviously, there is no single line for all cases, but the determination where the line is drawn must be based on the circumstances present in each case. In *Moore* v. *American United Life Ins. Co., supra,* 150 Cal. App. 3d 610, the court upheld awards with a ratio of 83 to 1 and noted the Supreme Court in *Neal* had upheld awards with a ratio of 78 to 1, and awards with a ratio of as much as 200 to 1 also had been upheld. (At p. 636.) The court in *Moore* noted that where a particular party's compensatory damages are modest but are the result of practices which have the potential of injuring others, "strong reliance on the reasonable relation rule may defeat the object and purpose of punitive damages," i.e., punishing and deterring such practices. (*Id.* at pp. 636-637.)

In *Downey Savings & Loan Assn.* v. *Ohio Casualty Ins. Co.* (1987) 189 Cal.App.3d 1072, review denied May 27, 1987, certiorari denied (1988) 486 U.S. 1036, the court declined to hold as a matter of law that punitive damages 32 times the compensatory damages were unreasonable. (189 Cal.App.3d at p. 1099.) Since the jury making the awards could reasonably have intended to punish the defendant not only for its conduct toward the plaintiff but also for its invidious practices—which could have affected others—in an effort to discourage the defendant from repeating those practices, the court gave the ratio of punitive to compensatory damages little weight. (*Ibid.*)

Here, one of the trial court's main purposes in increasing the punitive damages award over that made in the first trial was to deter future fraudulent conduct against others, since the original award had apparently been insufficient to encourage Shell to take any steps to make sure such fraudulent conduct did not recur. Under these particular circumstances, a ratio of punitive to compensatory damages of 17 to 1 is not as a matter of law unreasonable. (*Downey Savings & Loan Assn.* v. *Ohio Casualty Ins. Co., supra,* 189 Cal.App.3d at p. 1099; *Moore* v. *American United Life Ins. Co., supra,* 150 Cal. App.3d at pp. 636-637.)

III

Appellant asserts the trial court's punitive damages award also violates rights protected by the United States and California constitutions. We cannot agree.

Shell first claims California's "deferential passion and prejudice standard of review" deprives it of due process of law, relying on *Pacific Mut. Life Ins. Co.* v. *Haslip, supra,* 113 L.Ed.2d 1. In *Haslip,* the United States Supreme Court expressed concern that unlimited discretion "in the fixing of punitive damages may invite extreme results that jar one's constitutional sensibilities." (At p. 20.) However, it was of the opinion that "[a]s long as the discretion is exercised within reasonable constraints, due process is satisfied." (*Id.* at p. 21.)

As far as review of a punitive damages award, it noted that the Alabama Supreme Court, whose decision it was reviewing, provided an additional check on the jury's or trial court's discretion. It undertook a comparative analysis and applied the detailed substantive standards it had developed for evaluating punitive awards. (*Pacific Mut. Life Ins. Co.* v. *Haslip, supra,* 113 L.Ed. 2d at pp. 21-22.) "In particular, it makes its review to ensure that the award does 'not exceed an amount that will accomplish society's goals of punishment and deterrence.' [Citations.] This appellate review makes cer-

tain that the punitive damages are reasonable in their amount and rational in light of their purpose to punish what has occurred and to deter its repetition." (*Id.* at p. 22.)

The factors the Alabama Supreme Court looked at in reviewing a punitive damages award included whether there was a reasonable relationship between the award and the harm which had occurred and/or was likely to occur from the defendant's conduct, the nature of the defendant's conduct, the profitability of the defendant's conduct and the desirability of removing the profit, the defendant's financial position, the costs of litigation, and other criminal sanctions or civil awards resulting from the same conduct. (*Pacific Mut. Life Ins. Co.* v. *Haslip, supra,* 113 L.Ed.2d at p. 22.) The court concluded the application of these factors imposed "a sufficiently definite and meaningful constraint on the discretion of Alabama fact finders in awarding punitive damages," and review of the award ensured it was "not grossly out of proportion to the severity of the offense and [had] some understandable relationship to compensatory damages." (*Ibid.*)

The United States Supreme Court felt the consideration of these factors distinguished Alabama's system from those of Vermont and Maine, about which concern had been expressed in earlier Supreme Court opinions dealing with punitive damages. "In those respective schemes, an amount awarded would be set aside or modified only if it was 'manifestly and grossly excessive,' . . . or would be considered excessive when 'it evinces passion, bias and prejudice on the part of the jury so as to shock the conscience,' . . . ." (*Pacific Mut. Life Ins. Co.* v. *Haslip, supra,* 113 L.Ed.2d at p. 22, fn. 10, citations omitted.)

The California Supreme Court in *Adams* v. *Murakami, supra,* 54 Cal.3d 105 observed: "The California standard of review appears to be similar to those as to which the high court noted its concern. We have stated that a

punitive damages award will be set aside only when it 'is so grossly disproportionate as to raise a presumption that it is the result of passion or prejudice.' " (At pp. 118-119, fn. 9.) However, since the court in any event had decided the punitive damages award before it had to be set aside due to the absence of any evidence as to the defendant's financial condition, it declined to address the issue, stating: "[W]e need not now decide, and do not decide, whether the traditional California 'passion and prejudice' standard of review is constitutionally sufficient under *Haslip* . . . . Nor do we express any view on that issue." (*Id.* at p. 119, fn. 9.)

In California, the determination whether a punitive damages award " 'is so grossly disproportionate as to raise a presumption that it is the result of passion or prejudice' " (*Adams* v. *Murakami, supra,* 54 Cal.3d at pp. 118-119, fn. 9) is not made in a vacuum. (*Las Palmas Associates* v. *Las Palmas Center Associates, supra,* 235 Cal.App.3d at p. 1258.) The determination is based on the factors set forth in *Neal* v. *Farmers Ins. Exchange, supra,* 21 CaI.3d at page 928. (*Adams, supra,* at pp. 109-110.) These factors include the nature of the defendant's acts, the relationship between the punitive damages and the actual harm suffered as reflected in the amount of compensatory damages, and the defendant's financial condition. (*Neal, supra,* at p. 928.) All these factors are considered in light of the purposes of punitive damages awards—punishment and deterrence. (*Ibid.*)

The factors to be considered in California in evaluating punitive damages awards are similar to those which must be considered in Alabama. As with Alabama's, they provide a basis for ensuring "that the punitive damages are reasonable in their amount and rational in light of their purpose to punish what has occurred and to deter its repetition." (*Pacific Mut. Life Ins. Co.* v. *Haslip, supra,* 113 L.Ed.2d at p. 22.) They impose a "sufficiently definite and meaningful restraint on the discretion of [Cali-

fornia] fact finders in awarding punitive damages" and review with those factors in mind "ensures that punitive damages awards are not grossly out of proportion to the severity of the offense and have some understandable relationship to compensatory damages" (*Ibid.*) "In sum, the 'passion and prejudice' test affords . . . on appeal the same general degree of scrutiny as found in the Alabama review process. [Citation.] It is only when the award exceeds the amount needed to accomplish the goal of punishment and deterrence that an appellate court can conclude the jury acted on its passion and prejudice." (*Las Palmas Associates* v. *Las Palmas Center Associates, supra,* 235 Cal.App.3d at pp. 1258-1259, fn. omitted.) Therefore, California's review of punitive damages awards is not violative of the constitutional guarantees of due process. (Cf. *Haslip, supra,* at p. 23.)

Shell also argues the trial court violated its due process rights when it placed on Shell the burden of proving punitive damages should not be imposed and when it failed to articulate a rationale for more than doubling the punitive damages award from the first trial. As previously discussed, the trial court did neither of these things.

The judgment is affirmed.

SPENCER, P.J.

We concur:

ORTEGA, J.
MASTERSON, J.

APPENDIX C

Date March 31, 1992 DEPT. 19

SUPERIOR COURT OF CALIFORNIA
COUNTY OF LOS ANGELES

C 552 457

PEOPLE OF THE STATE OF CALIFORNIA

vs.

NELSON, EDWARD L., *et al.*,
and RELATED CROSS-ACTION

STATEMENT OF DECISION ON REMAND
FROM APPELLATE COURT

The above matter was remanded to the Superior Court for reconsideration and modification without necessity of further trial proceedings or receipt of additional evidence.

Court renders its Statement of Decision signed and filed this date.

Judgment is signed and filed this date.

A copy of this minute order and Statement of Decision and Judgment is sent via U.S. Mail this date to counsel addressed as follows:

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Marine Del Ray, CA 90292

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Gregory Horn, Esq.
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[Minutes Entered 03/31/92, County Clerk]

SUPERIOR COURT OF THE
STATE OF CALIFORNIA FOR THE
COUNTY OF LOS ANGELES

Case No. C 552 457

EDWARD L. NELSON,
Cross-Complaint
and Respondent,

vs.

SHELL OIL COMPANY,
Cross-Defendant
and Appellant.

JUDGMENT

[Filed Mar. 31, 1992]

The above entitled matter was remanded to the Superior Court for reconsideration and modification without necessity of further trial proceedings or receipt of additional evidence.

The court rendered its Statement of Decision signed and filed March 31, 1992.

Based upon reconsideration of the evidence.

IT IS ORDERED, ADJUDICATED AND DECREED AS FOLLOWS:

1. The cross-complainant Nelson Trust is awarded $268,891.00 as actual damages against cross-defendant Shell Oil Company with legal interest from October 26, 1990;

2. The cross-complainant Nelson Trust is awarded $4,600,000.00 as punitive damages against Shell Oil Company.

DATED: Mar 31, 1992

/s/ Arthur Baldonado
ARTHUR BALDONADO
Judge of the Superior Court

SUPERIOR COURT OF THE
STATE OF CALIFORNIA FOR THE
COUNTY OF LOS ANGELES

Case No. C 552 457

EDWARD L. NELSON,
Cross-Complainant
and Respondent,

VS.

SHELL OIL COMPANY,
Cross-Defendant
and Appellant.

STATEMENT OF DECISION

[Filed Mar. 31, 1992]

The Judgment of October 26, 1990, in this case was modified by the Court of Appeal by decision filed October 21, 1991. On remand this court was directed to modify actual damages to plaintiffs in the sum of $281,516.00 less a credit to defendants Shell Oil of $12,625.00 for a total of $268,891.00. Punitive damages had been assessed in the sum of $6,295,000 as detailed in the prior Statement of Decision. That amount has been set aside as excessive and the trial court directed to reconsider and reduce the amount without further evidence or trial.

The Appellate Court opinion noted that this court "interpreted the evidence in the second trial as establishing that Shell was continuing to utilize the manipulative techniques advanced in the Base Lease Manual" and that this conclusion was not supported by the evidence.

At the last trial plaintiffs subpoenaed "any and all writings or documents wherein Shell either modified, with-

drew, repudiated or otherwise prevented or discouraged the continued use of its Base Lease Manual or any part thereof." Shell produced no documents whatsoever relative to the categories sought, and stipulated that none existed. No official action was taken by defendants concerning the manual following the first trial. Robert Drager, real estate manager, contested the implications of such an absence. At the first trial Drager's deposition testimony showed he was provided with a copy of the base lease manual and directed to use it in his real estate work at his initial training seminar. He further testified that he used it as a guideline for negotiating service station leases. At the last trial Drager testified that he had not prepared any document discussing or modifying the use of the manual. Nor was he aware of any official notice from Shell Oil Company directed to Shell employees in California or elsewhere modifying or curtailing the practices advanced in the base lease manual. He testified he had not seen or used the manual since July 1987, and that he had not referred newer real estate personnel to the manual. He was unaware if a copy was on the premises.

Mindful of the directions of the court, this court will consider the evidence before it for appropriate conclusions and inferences to be reasonably drawn.

It is clear that following the first trial Shell undertook no official action to withdraw, modify or rescind the techniques they were using when negotiating service station leases. If there was to be some change in these practices it was not evidenced. It can be inferred from Drager's testimony that no such change had ever been thought of.

This is not to conclude that Shell did or did not continue to follow the principles advocated in the manual following the second trial. However, an inference may be fairly drawn that in the absence of any written directives

Shell undertook no meaningful or effective efforts to communicate any rescission of its prior policy as set forth in the manual. It is also reasonable to infer that in the absence of any written modification the persons in the field, who were negotiating service station leases, had not been clearly told to halt their use of methods of fraud advocated in the manual.

Drager testified there are older and younger real estate representatives. At a minimum it would be expected that if the punitive damage assessment from the first trial were to have any effect at all, the older representatives who were trained by using the base lease manual would be directed to avoid or discontinue using the fraudulent methods taught in the manual. Without some form of unequivocal notification that the old ways were to be discontinued, how can any objective observer be convinced there has been a change in practice? Some effort following the first trial to withdraw or recall the base lease manuals would be reasonably expected if the first punitive damage award was seen as anything beyond a mere nuisance. It is reasonable to infer from Drager's testimony that he was unaware of any effort to recall the manual. He testified that he did not know if a copy of the manual existed in the Anaheim office. If a recall effort had been ordered he should have known about it.

Shall also prepared a Condemnation Manual which told employees to keep abreast of developments when condemnation was to take place.

Suggestions were made to minimize a lease feature by hurrying, joking or grouping together and dismissing as unimportant the desired feaure, or how to effectuate inclusion of the "use the premises for any lawful purpose" phrase. It emphasizes the importance of timing in renewal negotiations, the advantages of placing the owner in a defensive position, and in a frustrated position. It directs the agent to be familiar with all instructions re-

lating to condemnation. It further suggests that when Shell wants to secure a long term lease from an owner who is middle-aged or slightly beyond to tell him or her that a long lease gives security of income for old age and to remind an owner that after a man dies, his family is always better off if it has a steady income and that it is very difficult to plan an estate on a short term lease.

These techniques and others should not be left in a state of ambiguity. By not rescinding such methods promptly and clearly Shell has at a minimum left the continued use of these methods up to the individual choice of field personnel, many of whom were trained to follow these techniques. It is obvious that the first assessment of punitive damages has been insignificant considering that one of the purposes of punitive damages is to deter future condct of a similar nature. It is clear that Shell has not accepted that such conduct is an unacceptable business practice. In assessing punitive damages the court is mindful of certain consideration. The more corrupt and cruel conduct the greater the amount should be. Shell's conduct is at the outer limits of intolerable business practice. The court also considers the public interest and the need to prevent this type of conduct. Considering the court's instructions to reassess punitive damage evidence in light of the opinion the Nelson Trust is awarded the sum of $4,600,000.00 in punitive damages. This amount for the reasons stated is the minimal amount that will deter future conduct and fairly and justly punish outrageous and fraudulent conduct. Few have an opportunity to lease a corner lot to an oil company, but the hundreds of Shell locations demonstrates the public need for defendants to change their leasing and condemnation practices. Others must learn by this example. Had the fraudulent conduct in question been the subject of criminal proceedings the criminal penalties would have been state prison sentences and multi-figure fines and penalties. Of course, Shell's fraund has not resulted in criminal sanctions and it is considered in mitigation. In obtaining

the Nelson lease extensions, the program outlined in Shell's Base Lease Manual were followed. Nelson, in good health, resisted Shell's efforts to continue the lease arrangement beyond May 31, 1986, although he was pressured to do so by Lewis for a period of three months in 1976. By 1976 the proposed Century Freeway and its impact on the Nelson Shell location due to condemnation was known to Shell because of their expertise and corporate resources in real estate activity. The Nelson lease still had in 1976 a ten year option extension to May 31, 1986, when Shell was pressuring the Nelson to grant them three five-year extensions.

In June of 1978 Shell accomplished its efforts to secure three 5-year extensions during a short meeting between Dale Lewis and Nelson under threat of collecting a $5,625 rent overpayment forthwith. At that time Nelson was suffering from advanced heart disease and senility. Shell knew of the Century Freeway condemnation and Nelson did not. The condemnation appraisal valued Shell's leasehold interest at $600,000.00 (Shell's expert witness) for their fraudulently obtained leasehold extensions and left Nelson some $300,000 for the property they owned in fee since 1942.

Another factor considered in assessing punitive damages against Shell is its wealth. A financial "slap on the wrist" of a wrongdoer in tantamount for no penalty at all. This is true in criminal justice and equally so in a civil case of serious wrongdoing. Shell's net worth is in the range of two billion dollars. One of the objectives of punitive damages is to punish the wrongdoer. For a punitive assessment to meet this objective and to be meaningful to such a prosperous company it must be substantial. Shell's financial statement makes clear that the punitive assessment herein will have no financially crippling effect on Shell. Indeed, the impact on Shell will be minimal compared to the harm done the now deceased Mr. Nelson and the aged Mrs. Nelson and Nelson trust.

The ratio between actual damages and punitive damages has also been considered. A ratio of 20 to 1 or less, as here, is appropriate and just given the reprehensibility of the conduct and the vulnerability of the victims coupled with their advanced age. When Shell obtained the lease options, Mr. Nelson was ill and 80 years of age. Shell was fully aware of the Nelson's need for retirement security and that the deal Nelson was induced to accept would undermine that security. The conduct should not be condoned in society.

The court cannot overstate its assessment of Shell's cold, ruthless plan to profit off the life savings of an elderly couple. In the absence of substatial punitive damages there would be no meaningful downside risk to Shell other than the litigation expense involved in moving the scheme forward to a conclusion. The profitability to Shell was substantial. Shell gave virtually nothing for the lease extensions, bore no risk and stood to take $600,000 from the Nelsons. If merely one effort creates such a gain the enticement of profitability would be too tempting to resist. The potential for enormous profit must be dampened by meaningful penalty if caught. The punitive assessment herein is intended to accomplish that result. Without the assessment of these punitive damages Shell or others have no risk other than litigation costs. Few landowners could resist the affluent tortfeasor knowing that litigation costs would be in the thousands of dollars. The public interest would be poorly served by such a result resulting in a denial of due process to the victim.

For the foregoing reasons the October 26, 1990, judgment of punitive damages is modified and reduced to $4,600,000.00.

DATED: Mar. 31, 1992

/s/ Arthur Baldonado
ARTHUR BALDONADO
Judge of the Superior Court

APPENDIX D

OFFICE OF THE CLERK
COURT OF APPEAL
STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT
JOSEPH A. LANE, CLERK

Division: 1 Date: 03/22/93

Munger, Tolles & Olson
Ronald L. Olson
355 S. Grand Avenue
Los Angeles, CA. 90071-1560

RE: Nelson, Edward L.

vs.

Shell Oil Company
2 Civil B067801
Los Angeles NO. C552457

THE COURT:

Petition for rehearing denied.

APPENDIX E

Date May 4, 1992 DEPT 19

SUPERIOR COURT OF CALIFORNIA
COUNTY OF LOS ANGELES

C 552 457

EDWARD L. NELSON,
Cross-Complainant
and Respondent

VS

SHELL OIL COMPANY,
Cross-Defendant
and Appellant

CROSS-DEFENDANT SHELL OIL COMPANY
MOTION TO VACATE JUDGMENT

Hearing date of May 12, 1992, for this motion is advanced and vacated.

Court makes its ruling without oral argument and on the papers submitted.

Court denies the motion.

A copy of this minute order is mailed vis U.S. Mail this date to counsel addressed as follows:

G. Dana Hobart, Esq.
O'Reilly & Hobart
4676 Admiralty Way Ste. 801
Marina Del Rey, CA. 90292

Munger, Tolles & Olson
355 So. Grand Ave.
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Mark Schreiber, Esq.
Schreiber & Horn, Inc.
16501 Ventura Blvd. Ste. 401
Encino, CA. 91436

[Minutes Entered 05/04/92, County Clerk]

APPENDIX F

2d Civil No. B 067801
LASC No. C 552457

No. ——

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

EDWARD L. NELSON, *et al.*,
Respondents,

v.

SHELL OIL COMPANY,
Petitioner.

Petition For Review Of Decision Of The
Court of Appeal For the State of California,
Second Appellate District, Division Four
[Case No. B067801]

TO THE HONORABLE MALCOLM L. LUCAS, CHIEF JUSTICE, AND TO THE HONORABLE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE STATE OF CALIFORNIA:

Petitioner, Shell Oil Company ("Shell"), defendant below, respectfully petitions this Court for review of any and all issues ruled upon by the Court of Appeal in the above entitled cause. A copy of the opinion filed on February 26, 1993 by the Court of Appeal, Second Appellate District, Division Four, is attached as Appendix A to this petition.

The Court of Appeal affirmed the trial court's judgment in favor of respondents Charlotte Nelson, et al., plaintiffs below, for $4,600,000 in punitive damages for alleged fraud in the context of a commercial lease of property.

ISSUES PRESENTED FOR REVIEW

1. Whether the California punitive damages system is invalid on its face and as applied here under the Due Process Clause of the Fourteenth Amendment to the United States Constitution ("Due Process Clause") because the California system grants excessive discretion to fact finders to award shifting, highly uncertain amounts of punitive damages through its subjective, ill-defined standards and an extremely deferential standard for reviewing punitive damages awards.

2. Whether the California punitive damages system is invalid under the Due Process Clause on its face and as applied here because it fails to apply objective criteria to ensure the fundamental fairness of punitive damages awards.

3. Whether the punitive damages award in this case violates California law and the Due Process Clause because the courts below increased punitive damages geometrically based on the plaintiffs' attorney's fees, for which plaintiffs were separately compensated.

I. STATEMENT OF THE CASE

The procedural history of this case is extraordinarily complex. This case now has seen decisions by three different panels of the Court of Appeal. Moreover, four different awards of punitive damages have been ordered; these awards have ranged in amount from the jury's original award of $235,600 to a high of $6.295 million. The current award, made by the trial court against Shell, stands at $4.6 million.

On June 18, 1985, the State of California filed a Complaint in Eminent Domain on a Los Angeles property located in the path of the well-publicized Century Freeway Project. The Complaint in Eminent Domain named the following defendants: Edward L. Nelson, Charlotte Louise Nelson; Edward L. Nelson and Charlotte Louise Nelson as trustees of the Nelson Trust (collectively "Nelson Trust"); and Shell Oil Company ("Shell"). Nelson Trust owned the fee interest in the property, while Shell owned a leasehold interest under a fixed-term lease.

On September 4, 1985, Nelson Trust answered the State's Complaint in Eminent Domain and filed a cross-complaint against Shell and others seeking rescission and restitution along with damages. Nelson Trust's primary allegation against Shell was that in negotiating several option agreements to extend the lease, Shell had not advised Nelson Trust of the planned construction of the Century Freeway and the resulting possibility that Nelson Trust's property would be condemned. One of Nelson Trust's contentions was that the base lease manual of Shell contained fraudulent and manipulative procedures to be used in negotiating commercial leases. At the time of the taking of Nelson Trust's property by the State, Shell had not yet exercised the lease extension options. At that time, Shell still possessed the property under its original lease, the validity of which was not in issue.

On July 27, 1987, the jury returned its verdict in favor of Shell on Nelson's Trust's claims for infliction of emotional distress and concealment of material facts with intent to defraud, but found Shell liable on a claim for intentional misrepresentation. The jury awarded plaintiffs $154,150 in actual damages, and $235,600 in punitive damages.

In addition to the causes of action heard by the jury, the trial court simultaneously heard Nelson Trust's equitable claim for rescission of the lease extension options.

The trial court rescinded the options. (*Nelson v. Shell Oil Company* (February 26, 1993) slip op. at 9-10.)

The trial court went on to award punitive damages against Shell on the rescission cause of action in the amount of $1,887,375 (calculated on the basis of $1.9 million, less $5,625 in rental overpayments made by Shell to Nelson Trust, and less $7,000 for the value of Shell's remaining leasehold which was taken by the State in the condemnation proceedings). Shell appealed from both the jury verdict and the trial court's judgment of rescission.

During the course of the appeal, Nelson Trust elected the remedy of rescission. The Court of Appeal affirmed the judgment of rescission but reversed the award of punitive damages on the ground that punitive damages cannot be awarded in the absence of actual damages, and no actual damages had been proved or awarded on the rescission count.

On remand, the trial court held a second trial, and over Shell's timely objection allowed Nelson Trust to offer evidence both of actual damages and of whether Shell had engaged in continuing wrongful conduct. The trial court then awarded $352,242 in general damages, the majority of which ($275,208) consisted of attorney's fees. The trial court also increased its original $1,887,375 punitive damages award over three-fold to $6.295 million. In addition to relying on evidence introduced at the first trial, the trial court based its second punitive damages award on the conclusion that Shell failed to withdraw the base lease manual following the first award of punitive damages. Shell appealed from the trial court's judgment.

On Shell's second appeal, the Court of Appeal upheld the trial court's decision to conduct a second trial on the issue of actual damages, but reduced the general damages award to $6,133 in lost interest income and $275,208 in

attorney's fees. (October 11, 1990 Trial Court Statement of Decision at 7, 18. (Joint Appendix In Support of Appellant's Opening Brief (hereinafter "App.") at pp. 54, 65); *Nelson v. Shell Oil Co.* (October 21, 1991) slip op. at 26 (App. at p. 199).) The Court of Appeal also reversed the trial court's $6.295 million punitive damages award, holding that there was no evidence from which to conclude that Shell continued to use the base lease manual or the procedures in it after the first award of punitive damages. (*Nelson v. Shell Oil Company* (February 26, 1993) slip op. at 14-15.)

The Court of Appeals instructed that on remand the trial court must "assess and award punitive damages consistent with the views expressed in this opinion." (*Id.* at 11.) The trial court was further instructed not to hold yet another trial. (*Ibid.*)

In its latest ruling, issued March 31, 1992, the trial court ordered that Shell pay $4.6 million in punitive damages to Nelson Trust. In making this final judgment, the trial court relied on the same factual conclusions that the Court of Appeals previously overturned as unsupported by the evidence. The trial court insisted that "in the absence of any written directives Shell undertook no meaningful or effective efforts to communicate any rescission of its prior policy as set forth in the manual," and speculated that "persons in the field" could still use the manual. (*Id.* at 16.)

Despite the internal inconsistency of the trial court's reasoning and its conflict with the Court of Appeal's October 1991 ruling, a different panel of the Court of Appeal on February 26, 1993 applied California's standardless, highly deferential "passion or prejudice" review and affirmed the trial court's award of $4.6 million in punitive damages. (*Nelson v. Shell Oil Company* (February 26, 1993) slip op.) In so ruling, the Court of Appeal adopted the trial court's internally inconsistent rea-

soning as its own. Forced to concede, in light of the ruling of the prior panel of the Court of Appeal in October of 1991, that there was no evidence that Shell continued to use the base lease manual, the Court of Appeal nevertheless ruled that the award was supported because there was no evidence that Shell had ceased use of the base lease manual by rescinding it in writing. (*Id.* at 16-18.) In addition, the Court of Appeal rejected Shell's constitutional challenges to the punitive damages award. (*Id.* at 26-31.)

On March 15, 1993, Shell filed a Petition for Rehearing, taking issue with the Court of Appeal's consideration of attorney's fees as part of actual damages for purposes of determining whether the ratio of punitive to actual damages was excessive. Shell pointed out that the ratio of the $4.6 million award to Nelson Trust's out of pocket loss of $6,133 is 750 to 1, orders of magnitude higher than the 17 to 1 ratio calculated by the Court of Appeal. The Court of Appeal denied the Petition for Rehearing on March 23, 1993.

II. PRELIMINARY STATEMENT

In this Petition for Review, Shell raises three issues, each concerning the requirements of the system for awarding punitive damages in California, and its constitutionality. The first issue presented here, the failure of California's system meaningfully to constrain fact finder discretion, is presently pending before this Court in four other cases. (See *MGW Inc. v. Frederick's Development Corp.* (1992) 12 Cal.App.4th 244, [6 Cal.Rptr.2d 888], *review granted* July 9, 1992 (case number G006654); *Gourley v. State Farm Mutual Automobile Ins. Co.* (1992) slip op. 1, *review granted* July 9, 1992 (S014133); *Wollersheim v. Church of Scientology* (1992) 4 Cal.App. 4th 1074, [6 Cal.Rptr.2d 532], *review granted* July 23, 1992 (case number B023193); *Hilgedick v. Koehring Finance Corp.* (1992) 4 Cal.App.4th 1074, [6 Cal.

Rptr.2d 532], *review granted* July 23, 1992 (case number A039723).) The other issues raised in this Petition also are fundamental to the California system, and should be considered by this Court at the same time that the first issue is resolved.

The second issue raised here is an additional challenge to the constitutionality of the punitive damage system in California, *viz.*, that the current system fails to ensure fundamental fairness in punitive damages awards in that it does not require consideration of objective indicia of fairness of such awards (such as the relationship of the award to other penalties for similar conduct). This issue now is pending before the United States Supreme Court in *TXO Production Corp. v. Alliance Resources Corp.* (1992) 187 W.Va. 457, [419 S.E.2d 870], *cert. granted*, 61 U.S.L.W. 3392-93 (argued March 31, 1993), and should be included as part of this Court's consideration of the constitutionality of the California punitive damages system

The third issue in this Petition presents this Court with the important issue of whether attorney's fees awards should be considered part of actual damages for purposes of calculating the ratio of punitive to compensatory damages. This is a recurring issue that is especially significant in cases where actual damages awards are low. Consideration of this case along with the others that have been granted review will allow a more comprehensive consideration of how courts should limit excessiveness of awards.

In the alternative, this Court should grant review and then hold this case so that it can be remanded for reconsideration after decision of the four cases that now are pending before this Court and that will be heard on the merits. The first issue raised here is identical to that which will be decided in these four cases and Shell should not be deprived of the benefit of this Court's ultimate ruling.

This case presents a perfect example of the failure of California's punitive damages system to comply with the dictates of due process and meaningfully constrain the arbitrary discretion of the fact finder. In this case, punitive damages truly have "run wild." (*Pacific Mutual Life Insurance Co. v. Haslip* (1991) 111 S.Ct. 1032, 1043, [113 L.Ed.2d 1, 20].) There have been four different amounts of punitive damages awarded in this case based on essentially the same evidence. A jury originally heard Nelson Trust's evidence of the alleged fraud by Shell in the negotiation of a commercial lease that underlies this case; that jury awarded Nelson Trust $235,600 in punitive damages. Yet Shell now comes before this Court with a $4.6 million punitive award having been ordered by a third judgment of the trial court and affirmed by the Court of Appeal. This Court should grant review to consider the validity of a punitive damages system that allows such disparity even within the confines of a single case.

This case also presents a perfect example of a grossly excessive punitive award. Independent of the procedures for assessing the award, it is so excessive that it cannot stand. It is well established that the United States Constitution's guarantee of fundamental fairness includes limits beyond which penalties may not go. (See *Haslip, supra,* 111 S.Ct. at p. 1045, [113 L.Ed.2d at p. 22]; *Seaboard Air Line Railyard v. Seegers* (1907) 207 U.S. 73, 78, [28 S.Ct. 28, 30, 52 L.Ed. 108, 110].)

The $4.6 million punitive award against Shell does not meet even the most minimal standards of fundamental fairness. The award bears no understandable relationship to the award by the jury, an independent fact finder in this same case, or to society's general policies toward the type of harm potentially caused by Shell's conduct. In addition, the punitive damages award against Shell far exceeds the bounds of any legislatively determined criminal or civil fine for similar conduct. Nor does the punitive award bear any understandable relationship to actual

damages. Despite the fact that Shell's action threatened only financial harm in a purely commercial setting, the ratio of punitive damages to actual damages is more than 750-to-1. This Court should grant review to delineate the appropriate standards for determining when a punitive damages award is excessive.

Finally, the punitive damages award in this case is invalid under California law and violates the Due Process Clause, because the Court of Appeal improperly included attorney's fees awarded Nelson Trust within compensatory damages when calculating the ratio of punitive to compensatory damages. As a result of this error, punitive damages against Shell have been inflated manyfold without reference to, and in utter disregard of, the purposes of punitive damages under California law.

The Courts of Appeal have had ample opportunity to address the important "federal constitutional dimension" of punitive damages in California in light of *Haslip*, but have left the system in its chaotic state. This Court already has recognized that the California system should be reviewed to resolve the question of its constitutionality —the question raised but reserved in *Adams v. Murakami* (1991) 54 Cal.3d 105, 118-119, fn.9, [284 Cal.Rptr. 318, 326-27, fn.9, 813 P.2d 1348, 1356-57, fn.9]. This Petition raises new issues that are of fundamental importance to this Court's constitutional inquiry. The Court should grant review of this case and fully address the insufficiencies of the California punitive damages system.

III. ARGUMENT

A. *California's System For Assessing Punitive Damages, On Its Face And As Applied In This Case, Violates Due Process By Virtue Of Its Subjective, Vague Criteria For Assessing Punitive Damages, And Deferential "Passion Or Prejudice" Standard For Reviewing Punitive Awards*

In *Haslip*, the United States Supreme Court held that while punitive damages are not *"per se"* unconstitutional, "unlimited jury discretion—or unlimited judicial discretion for that matter—in the fixing of punitive damages may invite extreme results that jar one's constitutional sensibilities." (*Haslip, supra*, 111 S.Ct. at p. 1043, [113 L.Ed.2d at p. 20].) Only if "the discretion is exercised within reasonable constraints . . . [is] due process . . . satisfied." (*Haslip, supra*, 111 S. Ct. at p. 1044, [113 L.Ed.2d at p. 21].)

The Supreme Court expressly warned in *Haslip* that the sufficiency of the punitive damages systems in certain states was suspect, singling out Vermont and Mississippi. "In those respective schemes, an amount awarded would be set aside or modified only if it was 'manifestly and grossly excessive,' or would be considered excessive when 'it evinces passion, bias and prejudice on the part of the jury so as to shock the conscience.' " (*Id.* at p. 1045, fn.10 (citations omitted).) In *Adams* this Court acknowledged the importance of *Haslip* and stated: "Although the high court upheld Alabama's punitive damages system . . ., the court expressed concern with less detailed state standards. . . . The California standard of review appears to be similar to those as to which the high court noted its concern." (*Adams, supra*, 54 Cal.3d at p. 118, fn.9.)[1]

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[1] Several post-*Haslip* decisions from outside of California already have concluded that pre-*Haslip* regimes for awarding punitive damages are inadequate to satisfy due process. (See *Johnson v. Hugo's Skateway* (4th Cir. 1991) 949 F.2d 1338, 1350-1351; *Garnes v.*

The California punitive damages system—including its standard of reviewing trial court awards of punitive damages—is virtually identical to the Vermont and Mississippi systems singled out for criticism by the Supreme Court in *Haslip*. As this court suggested in *Adams*, California's system of awarding punitive damages does not meet the requirements of *Haslip*.

"Punitive damages are an anomaly in our civil jurisprudence." (*Egan v. Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d 809, 825, [157 Cal.Rptr. 482, 598 P.2d 452] (Clark J., concurring and dissenting).) The purpose of punitive damages "is a purely public one. The public's goal is to punish wrongdoing" and thereby "to deter future misconduct." (*Adams, supra*, 54 Cal.3d at p. 110 (emphasis added).) However, unlike actions seeking criminal sanctions, punitive damages are pursued by private litigants and private attorney's who have no accountability to the public, are not constrained by standards applicable to public prosecutors, and who have a direct, material and substantial personal interest in attaining the greatest possible penalty in every case.[2] Furthermore, while "the civil law is concerned with . . . compensating persons for harm suffered" (*Egan, supra*, 24 Cal.3d at p. 825 (Clark J. concurring and dissenting)), punitive damages are exclusively extra-compensatory. "An award of punitive damages . . . is a boon for the plaintiff." (*Adams, supra*, 54 Cal.3d at p. 120.)

Fleming Landfill, Inc. (W. Va. 1991) 189 W. Va. 656 [413 S.E.2d 897]; *Alexander & Alexander, Inc. v. B. Dixon Evander & Associates, Inc.* (Md. Special App. 1991) 88 Md. App. 672, [596 A. 2d 687, 710], *cert. denied*, (Md. 1992) 605 A.2d 137.)

[2] (Cf. *Young v. United States ex rel. Vuitton et Fils.* (1987) 481 U.S. 787, 809, [107 S.Ct. 2124, 2138, 95 L.Ed.2d 740, 759] ("[c]ounsel for a party that is the beneficiary of a court order may not be appointed as prosecutor in a contempt action alleging a violation of that order").)

Under California law, fact finders are entrusted with extremely broad discretion to inflict punitive damages. "The channeling of just the correct quantum of bile to reach the correct level of punitive damages is, to put it mildly, an unscientific process complicated . . . by the lack of objective criteria from either the Legislature or the courts as to 'how much' is necessary to punish and deter." (*Devlin v. Kearny Mesa AMC/Jeep/Renault, Inc.* (1984) 155 Cal.App.3d 381, 388, [202 Cal.Rptr. 204].)

Moreover, the considerations pronounced in *Neal v. Farmers Insurance Exchange* (1978) 21 Cal.3d 910, 928, [148 Cal.Rptr. 389, 582 P.2d 980], provide no meaningful limitation on a fact finder's discretion. Pursuant to *Neal*, punitive damages are assessed by reference to three broad areas of inquiry: (1) the nature of the defendants' conduct; (2) the relationship of punitive damages to actual damages; (3) the defendant's financial position. (*Adams, supra*, 54 Cal.3d at p. 110 (holding that evidence going to each of these broad areas of inquiry is required, not optional).) Yet these criteria are, in turn, inherently highly subjective, as this case illustrates, and do not provide meaningful limits on punitive damages awards.

First, the nature of a defendant's conduct is an inherently subjective inquiry. One fact finder may perceive a set of facts as an arms-length commercial transaction between two relatively sophisticated parties, albeit one in which some overreaching may have occurred. Since such overreaching was purely limited to financial dealings and did not imperil life or limb, such a fact finder may conclude that a relatively modest punitive award is justified. Another fact finder, *based on precisely the same set of facts*, may react viscerally to a large corporation's commercial dealings with an individual and impose punitive damages in the millions.

This scenario is *precisely* what occurred in this case. The jury in this case awarded a sum of only $235,600 in punitive damages. The trial judge observed precisely

the same evidence as the jury, but apparently perceived a far more grievous wrong and awarded $1.9 million in punitive damages. After that $1.9 million award was overturned, the trial court attempted unsuccessfully to triple the $1.9 million award, and now has more than doubled that award.

Unlike the nature of defendant's conduct, the ratio of punitive damages to actual damages is not inherently subjective and might have evolved as a significant constraint on the subjective, arbitrary nature of punitive damages. But it has not so evolved in California. For example, in *Gagnon v. Continental Casualty Co.* (1989) 211 Cal. App.3d 1598, [260 Cal.Rptr. 305], the appellate court held that the relationship between compensatory and punitive damages has "little inherent meaning" and that a ratio of punitive to actual damages of "2,000 to 1 [has] been found reasonable." (*Id.* at 1604.) Indeed, in this very case the ratio of punitive damages to actual damages is 750 to 1. In light of the result in this case, it must be recognized that under current California law consideration of the ratio of punitive damages to actual damages imposes little restraint on the fact finder's arbitrary exercise of discretion.

Finally, California's requirement that evidence of financial condition be introduced is pernicious. Unlike the Alabama scheme at issue in *Haslip,* which precludes the fact finder from considering the defendant's wealth when calculating punitive damages,[3] the California system not only encourages but requires the fact finder to do so. As a result, plaintiffs like Nelson Trust are likely to "enjoy a windfall because they have the good fortune to have a defendant with a deep pocket." (*Haslip, supra,* 111 S. Ct. at p. 1045, [113 L.Ed.2d at p. 22].)

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[3] (See *Haslip, supra,* 111 S.Ct. at p. 1045, [113 L.Ed.2d at p. 22].) In Alabama, evidence of the defendant's financial condition is only admitted during the post-verdict hearing conducted by the trial judge to determine whether the award is excessive.

The extraordinarily broad discretion of California fact finders is not counter-balanced by meaningful judicial review. On appeal, "[a]ll presumptions favor the correctness of the verdict and judgment," (*Devlin, supra,* 155 Cal.App.3d at p. 388) and the trial court's determination that a punitive damages award is not excessive is "accorded great weight." (*Ibid.*) A "punitive damage award will be set aside only when it 'is so grossly disproportionate as to raise a presumption that it is the result of passion or prejudice.' " (*Adams, supra,* 54 Cal.3d at p. 118, fn.9 (quoting *Neal, supra,* 21 Cal.3d at p. 928).)

Although a court applying the California "passion or prejudice" standard for reviewing punitive awards takes account of the same general considerations as the fact finder—the reprehensibility of the defendant's conduct, the relationship of the punitive award to actual damages, and the relationship of the punitive award to the defendant's financial condition—it does so *only* to determine whether the jury acted out of "passion or prejudice." (*Neal, supra,* 21 Cal.3d at p. 928).[4] Moreover, as just discussed, the *Neal* considerations impose no meaningful constraint on the discretion of fact finders.

This case presents a classic example of the failure of California law to constrain a fact finder's discretion in assessing punitive damages. Even though the same facts have predominated throughout the history of this case, and the same trial judge has presided throughout, *this case has seen four awards of punitive damages, which*

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[4] The Alabama Supreme Court has recognized that an inquiry that is limited to a search for "passion or prejudice" does not provide adequate protection against an excessive award. " '[E]ven though a jury verdict may not be excessive because it is the result of an improperly functioning jury, it is possible for a verdict to be excessive even when it is the result of a properly functioning jury.' " (*Land & Associates, Inc. v. Simmons* (Ala. 1989) 562 So.2d 140, 150, *quoting Green Oil Co. v. Hornsby* (Ala. 1989) 539 So.2d 218, 222.)

have differed from each other by as much as 27 fold.[5] Indeed, the current punitive award is almost twenty times the jury's *original punitive award,* which was based on essentially identical facts.[6]

The Court of Appeal stated and applied California's lax "passion or prejudice" standard of review in affirming the trial court's latest $4.6 million punitive award; the trial court's decision could not have survived otherwise. The Court of Appeal's October of 1991 opinion held that an increase in punitive damages from the trial court's original $1.9 million award based on continuing bad acts by Shell was not justified because, "[i]t is equally reason-

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[5] The only new evidence since the jury's award of $235,600 in the original fraud action was evidence offered by Nelson Trust as to the possible continued use by Shell of its base lease manual after the first award of punitive damages. This evidence was so inconclusive that the Court of Appeal held in its October of 1991 opinion (reversing the trial court's award of $6.295 million in punitive damages), "[i]t is equally reasonable to conclude on the basis of what was testified to that Shell no longer uses the manual or the procedures it espouses." (*Nelson v. Shell Oil Company*, slip op. at 15 (February 26, 1993).)

[6] In addition, California's rudderless system for assessing punitive damages lends itself to abusive increases in punitive damages after a party exercises the right to appeal a prior judgment. Asserting a legitimate legal argument on appeal is simply not conduct that, consistent with due process, can be punished. (See, e.g. *Alabama v. Smith* (1989) 490 U.S. 794, 798-802, [109 S.Ct. 2201, 2204-06, 104 L.Ed.2d 865, 871-74] ("Where the sentencing judge who presides at both trials can be expected to operate in the context of roughly the same sentencing considerations . . . any unexplained change in the sentence is therefore subject to a presumption of vindictiveness [and is invalid].")) When making the third award of punitive damages the trial court operated in *precisely* the same context as when making the first award of punitive damages, save for evidence that the Court of Appeal in October of 1991 held to be insufficient as a matter of law to establish continuing misconduct. Thus, the over $2.7 million increase in punitive damages represented by the trial court's third award violated Shell's right to due process of law.

able to conclude on the basis of what was testified to that Shell no longer uses the manual or the procedures it espouses." (*Nelson v. Shell Oil Company* (February 26, 1993) slip op. at 15.) Nevertheless, the February of 1993 Court of Appeal decision upheld the trial court's increase in punitive damages on the ground that there was a "possibility Shell real estate representatives would continue to use" the manual. (*Id.* at 18.) On the basis of this nonexistent "distinction"—Shell, as a corporation, of course can act only through its "representatives"—the original punitive damages award was more than doubled. In short, only the most deferential review could preserve the present award in light of the previous decision of the Court of Appeal. California's subjective, contentless criteria for assessing punitive damages and lax standards for reviewing punitive damages awards have deprived Shell of due process.

B. *California's System For Awarding Punitive Damages Fails To Apply Objective Criteria To Ensure The Fundamental Fairness Of Punitive Damages Awards As Required By The Due Process Clause*

Clearly, there are constitutional limits on excessive penalties "beyond which penalties may not go." (*Seaboard Air Line Ry. v. Seegers, supra*, 207 U.S. at p. 78, [28 S.Ct. at p. 30, 52 L.Ed. at p. 110]. See also *St. Louis Iron Mountain & S. Ry. v. Williams* (1919) 251 U.S. 63, 66-67, [40 S.Ct. 71, 73, 64 L.Ed. 139, 141] ("That [the Fourteenth Amendment] places a limitation upon the powers of the States to prescribe penalties for violations of their laws has been fully recognized"); *Standard Oil Co. v. Missouri* (1912) 224 U.S. 270, 286, [32 S.Ct. 406, 411, 56 L.Ed. 760, 769] (due process guarantees that courts may "no more assess excessive damages than . . . impose excessive fines").) Accordingly, the courts for nearly a century have scrutinized extra-compensatory penalties to ensure that they are not "so grossly excessive

as to amount to deprivation of property without due process of law." (*Waters-Pierce Oil Co. v. Texas* (1909) 212 U.S. 86, 111, [29 S.Ct. 220, 227, 53 L.Ed. 417, 430].)

It is therefore unsurprising that the Supreme Court, acting on its "concern about punitive damages 'run wild'" (*Haslip, supra,* 111 S.Ct. at p. 1043, [113 L.Ed.2d at p. 20]), confirmed that there are limits beyond which punitive damages awards may not go. (*Ibid.*) ("general concerns of reasonableness . . . properly enter into the constitutional calculus"). The Court recognized in *Haslip* that a punitive damages award of "more than 4 times the amount of compensatory damages" may be "close to the [constitutional] line." (*Id.* at 1046.)

The $4.6 million penalty assessed against Shell is so clearly excessive and strays so far from the traditional notions of fairness established by "history and wide practice" (see *Schad v. Arizona* (1991) 111 S.Ct. 2491, 2500, [115 L.Ed.2d 555, 569] (plurality opinion)) that it violates "fundamental fairness . . . [and] the rationality that is an essential component of that fairness." (*Ibid.*) The Court of Appeal applied no objective criteria to ensure the fairness of the award in light of the policies of the State of California.

The Supreme Court long has noted the "importance of history and widely shared practice as concrete indicators of what fundamental fairness and rationality require." (*Id.* at 2501.) Thus, the fundamental fairness determination is properly informed by such objective indicia of fairness as (1) awards upheld against the same defendant in the same case by another, independent trier of fact; (2) society's general policies toward the harm potentially caused by the conduct at issue; (3) legislative penalty decisions with respect to similar conduct; and (4) the relationship of punitive damages to actual damages. Tested against

these objective standards, the $4.6 million award is clearly excessive.

The jury in this same case heard all of the evidence heard by the trial court (with the exception of the extremely equivocal testimony in the second trial concerning whether there was any continuing use of Shell's "base lease" manual). The jury awarded $235,000 in punitive damages, *less than one-nineteenth* the amount of the trial court's $4.6 million punitive award. This type of disparity within the same case based on very similar evidence is simply untenable.

In addition, the misconduct alleged here involved neither violence nor threat of violence to any person. It is beyond doubt that where punishment is concerned, society is far more protective of people than property. (See, e.g., *Solem v. Helm* (1983), 463 U.S. 277, 292-93, [103 S.Ct. 3001, 3010-11, 77 L.Ed.2d 637, 650-51]; *Eisert v Greenberg Roofing & Sheet Metal Co.* (Minn. 1982) 314 N.W.2d 226, 229 (decision to deny punitive awards in strict liability actions where injury is limited to property damage "reflects the higher value our society places on the safety of persons than it does on the security of property"); *Slough v. J.I. Case Co.* (Kan. Ct. App. 1982) 650 P.2d 729, 736 (reducing punitive award because "there was a very minimum of evidence to indicat[e] a danger of physical injury to persons as a result of [appellant's] conduct").) No dangerous or potentially dangerous instrumentality was involved. No person's honor, dignity, or reputation was harmed or even threatened. This case involves a lease of commercial property.[7] Shell's conduct could threaten only financial harm.

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[7] (See *Alexander & Alexander, supra*, 596 A.2d at p. 710 (jury awarded $250,000 in compensatory damages and $40 million in punitive damages; trial court remitted punitive damages to $12.5 million. Court of Appeal vacated and remanded for a new trial, observing "[t]his was, at bottom, a commercial dispute between two business competitors").)

Moreover, Shell's punishment far exceeds any legislatively determined punishment for such conduct. Legislative judgments are particularly valuable guides to proportionality, because the legislature is responsible for establishing the entire scheme of civil and criminal sanctions. In numerous statutes the California legislature has established a fine of $10,000 to punish criminal fraud threatening purely financial harm. (See Cal. Civ. Code, §§ 1695.8, 1812.217, 2924h(g).)[8] The fines authorized by these statutes do *not* depend no the wealth of the defendant. Shell, which has never been charged with any criminal conduct, has been "fined" 460 times as much by the trial court as the legislature has deemed appropriate for *criminal* fraud, apparently primarily because wealth is considered in California when assessing punitive damages.

Nor does the challenged award bear any "understandable relationship to compensatory damages." (See *Haslip, supra*, 111 S.Ct. at p. 1045, [113 L.Ed.2d at p. 22].) In *Haslip*, the Supreme Court observed that a punitive award of four times compensatory damages was "close to the [constitutional] line." (111 S.Ct. at p. 1046, [113 L.Ed.2d at p. 22].) In the instant case, the ratio of punitive to actual damages is 750 to 1.

Fundamental fairness review, like most constitutional exercises, may not admit of bright-line distinctions. Here, however, all of the relevant objective indicia demonstrate that the $4.6 million award against Shell strays far beyond any traditional notions of fairness established by history and wide practice. The Court of Appeal ignored these objective criteria and in doing so affirmed an award that exceeds the bounds of contemporary and historical practice by *orders of magnitude*. This Court should grant review to establish the objective standards necessary to

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[8] Each of these stautes provide that as an alternative or additional penalty the offender may be sentenced to jail or prison for a maximum of 1 year.

ensure constitutionally required fundamental fairness in imposing punitive damages penalties.

C. *The Treatment Of Attorney's Fees By The Courts Below When Assessing Punitive Damages Was Wholly Improper; The Courts' Failure To Follow California Law Is An Error Of Constitutional Dimension*

This case also presents this Court with the opportunity to resolve the important, unsettled question whether an attorney's fees award properly is included within "compensatory damages" when calculating the ratio of punitive to actual damages. Adding attorney's fees to a plaintiff's out of pocket loss for purposes of the punitive damages comparison (as the Court below did) is contrary to the purposes of punitive damages awards in California.

In this case, the actual damages awarded to Nelson Trust consisted of a very modest award of $6,133 in lost interest income. (October 11, 1990 Trial Court Statement of Decision at 18 (App. at 65); *Nelson v. Shell Oil Co.* (October 21, 1991) slip op. at 26 (App. at 199).) Thus the ratio of punitive to actual damages is $4.6 million to $6,133 or approximately 750 to 1. Nelson Trust also was awarded attorney's fees (erroneously, as discussed below) in the amount of $275,208. (October 11, 1990 Trial Court Statement of Decision at 7 (App. at 54); *Nelson v. Shell Oil Co.* (October 21, 1991) slip op. at 26 (App. at 199).) It is only by adding the attorney's fees award to actual damages that the Court of Appeal obtained a ratio of punitive to actual damages of 17 to 1.

But adding attorney's fees to the actual damages award for purposes of considering the ratio of punitive to actual damages is contrary to California's articulated criteria for calculating punitive damages. (See, e.g., *Adams, supra*, 54 Cal.3d at p. 110 (setting forth the criteria against which punitive damages awards are reviewed).) As the

following discussion shows, where, as in California, a punitive damages award is required to be proportional to the *actual harm done to the victim*, an attorney's fees award should not be included in the actual damages part of the ratio and, indeed, the permissible ratio of punitive to actual damages should be *lower* than in a case where the plaintiff was not compensated for attorney's fees. Where a plaintiff has received payment for his attorney's fees, the harm caused to him is no greater than if there had been no attorney's fees award. Indeed the plaintiff who receives a fee award already has been compensated beyond the actual harm done to him because he has been reimbursed for the cost of the lawsuit to vindicate his rights.

A simple example illustrates these principles. Suppose in a tort action, case 1, the plaintiff is awarded $10,000 in actual damages and the court finds that a ratio of punitive to actual damages of two-to-one is appropriate, awarding $20,000 in punitive damages. In a similar tort action, case 2, the plaintiff is awarded the same $10,000 in actual damages plus an additional $20,000 in attorney's fees. Assuming all else to be equal (the defendants' conduct, wealth, etc.), the plaintiff in the second case surely is not entitled to a $60,000 punitive damages award based on a two-to-one ratio of punitive damages to actual damages plus attorney's fees. It is absurd to suggest that the plaintiff in the second case suffered greater harm than the plaintiff in the first case. (See *Amica Mutual Ins. Co. v. Schettler* (Utah Ct. App. 1989) 768 P.2d 950, 967 (attorney's fees "go on neither side of the scale when determining whether the amount of punitive damages awarded 'bear[s] a reasonable relation' to the amount of general damages"). Cf. *Viner v. Untrecht* (1945) 26 Cal.2d 261, [158 P.2d 3] (punitive damages cannot include attorney's fees).)

As stated in the Court of Appeal's opinion, under current California law punitive damages "must bear a

reasonable relationship to the amount of harm actually suffered." (*Nelson v. Shell Oil Company* (February 26, 1993) slip op. pp. 21-22. See also *Las Palmas Associates v. Las Palmas Center Associates* (1991) 235 Cal.App.3d 1220, 1257, [1 Cal.Rptr.2d 301] (punitive damages must bear a reasonable relationship to the injury, harm or damage actually suffered).) The Court of Appeal's consideration of the punitive damages ratio fails to assure that the punitive damages award bears any rational relationship to the extent of the harm suffered by the plaintiff. As calculated by the Court of Appeal, the "harm" (actual damages) component of the punitive damages ratio consists almost entirely of attorney's fees. Yet the amount of fees rung up by a plaintiff's lawyers may have little or no relationship to the harm caused by the defendant's conduct. A defendant has no control over the energy and resources a plaintiff chooses to bring to bear in litigation. Nor does a defendant control the fees charged by a plaintiff's attorneys.

For example, if Nelson Trust's attorneys had charged $1 million in fees, the line of reasoning of the Court of Appeal would sustain a requirement that Shell pay the $1 million as part of compensatory damages, while in addition paying a punitive damages award of approximately $17 million. Yet, Shell's conduct would not have been any different, Nelson Trust would have suffered no more real-world harm, and Nelson Trust again already would have received its costs of litigation before any punitive damages were awarded.

Moreover, when a court considers the amount of harm to the plaintiff in determining the appropriate size of a punitive damages award, the court should take into account whether or not the plaintiff already has been compensated for the "harm" of incurring litigation expense to vindicate his rights. In the hypothetical situation described above, the plaintiffs in cases 1 and 2 suffered the same amount of harm. In case 2, before the award of

punitive damages, the plaintiff was compensated for the harm done by the defendant's wrongful act *and* for the cost of obtaining reimbursement for that harm (the attorney's fees award).

In light of California's criteria for awarding punitive damages, a court considering the appropriate size of a punitive damages award should take into account that in case 2 the plaintiff already has been compensated for the "harm" of incurring litigation expenses and should award a lesser amount of punitive damages than in a comparable case with no fee award. Including attorney's fees in the actual damages component of the punitive damages ratio, as the Court of Appeal has done, produces *precisely the opposite effect*. It is irrational to measure the excessiveness of a punitive damages award by considering "harm" to the plaintiff in case 1 without reference to the cost of vindicating rights but to consider "harm" in case 2 as including the costs of bringing and prosecuting the lawsuit. Thus the "excessiveness" calculus engaged in by the Court of Appeal did not assure adherence to California's criteria for determining punitive damages.

Indeed, by including attorney's fees in its calculation of the punitive damages ratio and inflating punitive damages solely based on attorney's fees, the Court of Appeal violated the spirit, if not the letter, of *Viner v. Untrecht*, *supra*, 26 Cal.2d at p. 273. In *Viner* this Court held that punitive damages cannot be increased on a dollar-for-dollar basis to compensate a plaintiff for attorney's fees. Yet by incorporating attorney's fees within the denominator of the punitive to actual damages ratio, the Court of Appeal artificially has reduced the ratio, and thereby has inflated the award of punitive damages. As demonstrated above, the Court of Appeal has gone far beyond the result rejected in *Viner*—a dollar-for-dollar increase—by increasing punitive damages *geometrically* solely based on attorney's fees. The perverse result of the Court of

Appeal's treatment of attorney's fees is to give plaintiffs and their attorneys every incentive to compile the largest reasonable amount of fees; there will be more than a dollar increase in punitive damages for every dollar increase in attorney's fees.

Had the Court of Appeal followed the logic of *Viner* and recognized that the proportion of punitive to actual damages is properly expressed as a ratio of 750 to 1, it would have been clear that this ratio was more than three and one-half times the largest ratio mentioned in the precedents cited by the Court of Appeal. Even under California's current inadequate system for assessing punitive damages the award against Shell was excessive.

The prejudice to Shell from the Court of Appeal's improper treatment of the punitive to actual damages ratio is compounded because under prevailing California law attorney's fees should not have been awarded to Nelson Trust in the first place. California law is clear that, as a general matter, a plaintiff is not entitled to recover attorney's fees incurred in bringing a fraud or rescission action. (Cal. Code Civ. Proc., § 1021; *Gray v. Don Miller & Associates, Inc.* (1984) (35 Cal.3d 498, 506, [198 Cal.Rptr. 551, 674 P.2d 253]; *Bezaire v. Fidelity and Deposit Co. of Maryland* (1970) 12 Cal.App.3d 888, 907, [91 Cal.Rptr. 142].) Nevertheless, in its second statement of decision the trial court awarded Nelson Trust its attorney's fees incurred in suing Shell for fraud and for rescission of the lease extensions that underlie this dispute.

The "tort of another" theory under which the Court of Appeal affirmed the trial court's award of attorney's fees in its October 1991 opinion is inapposite. The "tort of another" exception to the general rule that an attorney's fees cannot be awarded only allowed a plaintiff to be awarded those fees that result from "the party seeking attorney's fees [being] required by the wrong of the defendant to protect his interests by bringing or defend-

ing an action *against a third person.*" (*Gray, supra,* 35 Cal.3d at pp. 508-09 (emphasis added).) The tort of another theory does not support the trial court's award of attorney's fees here as those fees consisted entirely of amounts expended by Nelson Trust *in pursuing its counterclaim against Shell.*[9]

The Court of Appeal's errors in the treatment of attorney's fees are of Constitutional dimension. The United States Supreme Court's decision in *Haslip* requires that a state's procedures for determining a punitive damages award must assure that "punitive damages are reasonable in their amount and *rational in light of their purpose* to punish what has occurred and to deter its repetition." (*Haslip, supra,* 111 S.Ct. at pp. 1044-45, [113 L.Ed.2d at pp. 21-22] (emphasis added).) Yet the Court of Appeal's consideration of the ratio of punitive to actual damages was arbitrary and irrational in light of California law and California's articulated purposes for awarding punitive damages.

If punitive damages awards are to be "rational" rather than wholly arbitrary a state must, at a minimum, follow its own well-established procedures for assessing and reviewing punitive damages awards. Yet in this case the California courts have failed to follow California law in their treatment of attorney's fees. As a result, Shell has been deprived of its right to due process.

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[9] The trial court stated: "*Nelson was required to litigate with Shell* beyond October 10, 1986 because the state would not otherwise release the $624,533.78 [the portion of the value of the subject real property, which had been condemned by the state, for which the state had not yet paid]. . . . Attorney fees in the amount of $275,208.00 were necessary and reasonably incurred by Nelson from October 10, 1986 through the trial which [against Shell] concluded in July 1987." (October 11, 1990 trial court Statement of Decision at 7 (App. at 54) (emphasis added).) Clearly the trial court awarded Nelson Trust attorney's fees that were incurred exclusively in litigating *this case against Shell.*

IV. CONCLUSION

For the foregoing reasons this Court should grant the Petition for Review and reverse the judgment below. In the alternative this Court should grant the Petition for Review and hold the case for eventual remand for consideration in light of the decision of this Court in *MGW*, *Gourley*, *Wollersheim*, and *Hilgedick*.

DATED: April 7, 1993

Respectfully submitted,

MUNGER, TOLLES & OLSON

By /s/ Carolyn B. Kuhl/PDH
CAROLYN B. KUHL

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and Petitioner
Shell Oil Company

[Proof of Service by Mail Omitted in Printing]

LIST PURSUANT TO
UNITED STATES SUPREME COURT RULE 29.1

1. Parent companies of Shell Oil Company

Royal Dutch Petroleum Company
Shell Petroleum Inc.
The Shell Transport and Trading Company, p.l.c.

2. Subsidiary/Affiliate Companies (except wholly owned) of Shell Oil Company

Agripro Biosciences Inc.
Al Furat Petroleum Company
Butte Pipe Line Company
CRI Europe S.A.
CRI Far East Trading Company Limited
CRI International, Inc.
CRI Investment Corporation
CRI Real Estate, Inc.
CRI-SAM, Ltd.
CRI Ventures, Inc.
CRI Zeolites Inc.
Catalyst Recovery Canada, LTD
Catalyst Recovery Europe S.A.
Catalyst Recovery of Louisiana, Inc.
Catalyst Technology, Inc.
Catalyst Technology (Canada) Ltd.
Catalyst Technology Europe S.A.
Catalyst Technology GmbH
Columbia LNG Corporation
Cortez Capital Corporation
Criterion Catalyst Company
Dixie Pipeline Company
East Texas Salt Water Disposal Company
Explorer Pipeline Company
Fractionation Research, Inc.
Grande Ecaille Land Company, Inc.
GRAVCAP, Inc.
Heat Transfer Reseach, Inc.

Inland Corporation
Locap, Inc.
Loop, Inc.
Lucky Chance Mining Company, Inc.
Mesbic Financial Corporation of Houston
Nippon CRI, LTD.
Oil Companies Institute for Marine Pollution Comp
Oil Insurance Limited
Pecten Angola Ltd.
Pecten Angola Exploration Ltd.
Pecten Bolivia Ltd.
Pecten Cameroon Company
Pecten Indonesia Misool Ltd.
Pecten Middle East Services Company
Pecten Suriname Ltd.
Plantation Pipe Line Company
Plumbing Claims Group, Inc.
Premix E.M.S. Inc.
Saudi Petrochemical Company
Shell Frontier Exploration Inc.
Shell Frontier Oil & Gas Inc.
Shell Frontier Services Inc.
Taranaki Offshore Petroleum Company Limited
United Scientific Incorporation
Van Salt Water Disposal Company
West Shore Pipe Line Company
Wolverine Pipe Line Company
Wyoming Industrial Development Corporation
Zeigler Coal Holding Company